KL

No. 84-1274

In the Supreme Court of the United States

OCTOBER TERM, 1984

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM

v.

DIMENSION FINANCIAL CORP., ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

JOINT APPENDIX

JOHN D. HAWKE, JR.
Counsel of Record
LEONARD H. BECKER
DOUGLAS L. WALD
ARNOLD & PORTER
1200 New Hampshire Avenue, N.W.
Washington, D.C. 20036
(202) 872-6700

Counsel for Respondents American Financial Services Association, Household Finance Corporation, and First Bancorporation

MICHAEL BRADFIELD
JAMES V. MATTINGLY, JR.
Counsel of Record
RICHARD M. ASHTON
BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
20th & C Streets, N.W.
Washington, D.C. 20551
(202) 452-3750

Counsel for Petitioner Board of Governors of the Federal Reserve System

(Appearances continued on inside front cover)

PETITION FOR CERTIORARI FILED FEBRUARY 6, 1985
CERTIORARI GRANTED APRIL 29, 1985

JEFFREY S. DAVIDSON
Counsel of Record
DENNIS M. GINGOLD
GLENN SUMMERS
HARRY J. KELLY
KIRKLAND & ELLIS
655 Fifteenth Street, N.W.
Washington, D.C. 20005
(202) 879-5000

Counsel for Respondents Dimension Financial Corporation, Daniel T. Carroll, Harold D. Dufek, William L. Mitchell, Ronald L. Shaffer, and A. Gary Shilling

THOMAS B. RIDGLEY
Counsel of Record
VORYS, SATER, SEYMOUR AND PEASE
52 East Gay Street
P.O. Box 1008
Columbus, Ohio 43216
(614) 464-6400

Counsel for Respondents Ohio Deposit Guarantee Fund, Horizon Savings & Loan Company, Horizon Service Corporation and Permanent Savings & Loan Association

ANTHONY J. CELEBREEZE, JR.
JOEL S. TAYLOR
Counsel of Record
ATTORNEY GENERAL OF OHIO
State Office Tower, 17th Floor
30 East Broad Street
Columbus, Ohio 43215
(614) 466-4320

Counsel for Respondents State of Ohio and Ohio Division of Savings & Loan Associations

LOUIS A. HELLERSTEIN
Counsel of Record
STEPHEN A. HELLERSTEIN
HELLERSTEIN, HELLERSTEIN & SHORE, P.C.
1139 Delaware Street
P.O. Box 5637
Denver, Colorado 80217
(303) 573-1080

Counsel for Respondents Colorado Industrial Bankers Association and Ft. Lupton, Monroe, Castle Rock and Ark Valley Industrial Banks

JAMES D. BLOUNT, JR.
Counsel of Record
JOHN L. JERNIGAN
R. MARKS ARNOLD
SMITH, ANDERSON, BLOUNT, DORSETT, MITCHELL & JERNIGAN
Post Office Box 12807
Raleigh, North Carolina 27605
(919) 821-1220

Counsel for Respondent Financial Institutions Assurance Corporation

In the Supreme Court of the United States

OCTOBER TERM, 1984

No. 84-1274

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, PETITIONER

v.

DIMENSION FINANCIAL CORPORATION, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

TABLE OF CONTENTS*

---

* The opinion of the court of appeals and the supplementary information appendix accompanying the final regulation adopted by the Board of Governors of the Federal Reserve System are reproduced as appendices to the petition for certiorari and are not reprinted here.

FEDERAL RESERVE SYSTEM
12 CFR Part 225
[Docket No. R-0470]
Bank Holding Companies and Change in Bank Control; Revision of Regulation Y

BEFORE THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

DATE	DESCRIPTION
May 19, 1983	Notice of proposed rulemaking issued by Board of Governors
May 25, 1983	Notice of proposed rulemaking published in Federal Register
July 18, 1983	Comment period expires
Dec. 29, 1983	Final rule approved by order of the Board of Governors
Jan. 5, 1984	Notice of final rulemaking published in Federal Register
Feb. 6, 1984	Effective date of substantive provisions of final rule

General Docket 83-2696

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

Petition for Review of an Order of the
Board of Governors of the Federal Reserve System

Case No. 83-2696

Consolidated with 84-1011, 84-1122, 84-1257 & 84-1270
For the Purpose of Record, Briefing, Argument &
Submission. Also 84-1407

Filed 12/30/83

DIMENSION FINANCIAL CORPORATION, DANIEL T. CARROLL, HAROLD D. DUFEK, WILLIAM L. MITCHELL, RONALD L. SHAFFER, AND A. GARY SHILLING, PETITIONERS

vs.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, RESPONDENTS

ATTORNEYS FOR APPELLANT

(A) THOMAS H. DUNCAN
Kirkland & Ellis

(A) DENNIS M. GINGOLD
(A) JEFFREY S. DAVIDSON
(A) DAVID K. PERDUE
(A) GLENN SUMMERS

For: State of Ohio & Huddleston in 84-1270

( ) CONNIE J. HARRIS
Ohio Attorney General

(X) ANTHONY J. CELEBREZZE, JR.
Attorney General, State of Ohio

(A) JAMES D. BLOUNT, JR.
(A) JOHN L. JERNIGAN
SMITH, ANDERSON, BLOUNT, DORSETT, MITCHELL & JERNIGAN
(A) R. MARKS ARNOLD

ATTORNEYS FOR APPELLEE

(A) RICHARD M. ASHTON
Board of Governors of the Federal Reserve System

12/30/83	CS. DKT.P.RVW. Case docketed; Petition for review of an agency order orig & 3 cc.
1/14/84	NAPR. F. Notice of appearance filed by Gingold, Duncan, Davidson, Perdue and Summers as attys. for Petitioners *
*1/16/84	NAPR.F Notice of appearance filed by R.M. Ashton as atty. for respondent
2/9/84	*ROA.F.* Record on appeal filed, (Certified Index) orig
2/16/84	M.F.ANY. F. Petitioners' motion for order initiating transfer of proceedings filed (orig & 6cc,c/s)
2/27/84	M.F. ANY. RES. F. Respondent's response to petitioners' motion for order initiating transfer of proceedings filed, orig. & 3cc,c/s.
2/24/84	M.CON.F—petitioners' in 84-1011 & 84-1122 motion to consolidate 83-2696, 84-1011, 84-1122 filed—orig. & 3 cc.—c/s
2/24/84	M.EXP.SCH.O.F-petitioners' in 84-1011 & 84-1122/motion to set expedited scheduling order in the three cases—orig. & 3 cc.—c/s (combined with above motion
3/1/84	*ROA.F.* Record on appeal filed, Vols. I-V (pleadings) (1870 pp.) Original (1870 tpp.)
2/27/84	M.EXTM.BR.F. Petitioners' motion for extension of time to file briefs filed, orig. & 6cc,c/s.
	M. CON. RES. F. Petitioners' response to motion of petitioners' in 84-1011 and 84-1122 to consolidate 83-2696, 84-1011, 84-1122 filed, orig. & 3cc, c/s (response incl. w/motion for extension of time to file brief)
	M.EXP. SCH. O. RES. F. Petitioners' response to petitioners' (in 84-1011 and 84-1122) motion for expedited scheduling order filed, orig. & 3 cc, c/s (incl. w/motion for extension of time to file brief and response to motion to consolidate filed above)
3/5/84	MEMO. IN SPT. F. Memorandum in support of motion to consolidate petitions for review (83-2696, 84-1011, 84-1122) and to set accelerated briefing and argument schedule filed by petitioners in 84-1011, 84-1122, orig. & 3cc,c/s.

3/1/84 M. CON. RES. F. Respondent's response to motion of petitioners in 83-269 84-1011 and 84-1122 to consolidate petitions for review filed, Orig. & 3cc., c/s.

M.EXP.SCH.RES.F. Respondent's response to petitioner's motion for expedited scheduling filed, Orig. & 3cc., c/s.

3/19/84 M. CON. DISP Granted Petitioner's motion to consolidate cases 84-1011, 84-1122, 83-2696, 84-1257 and 84-1270 disposed of by McKay and Seymour. Parties served by mail.

M. EXP. SCH. O. DISP Granted petitioner's motion to set an accelerated briefing schedule disposed of by McKay & Seymour. Parties served by mail.

O. RMK The petitioners in No. 83-2696 are designated as leading the briefing of this matter for all petitioners disposed of by McKay & Seymour. Parties served by mail.

O.ASGN.CAL Order assigned to Calendar B—Seth. Parties served by mail.

O.BR.DUE Petitioners' lead brief is due 4/9/84. Other petitioners may file statements of joinder and adoption of the lead brief or distinction of their positions in no more than 10 pages each within 10 days thereafter. A joint brief is strongly encouraged. Duplicative arguments will not be favored. Respondent may file a brief of no more than 75 pages within 21 days of service of petitioner's brief. Lead petitioners may file a reply brief within 10 days of service of respondent's brief. Other petitioners may file separate reply briefs of no more than 5 pages each if necessary within 7 days of service of the lead brief disposed of by McKay & Seymour. Parties served by mail.

NAPR.F. Notice of appearance filed by Harris as attorney for petitione State of Ohio and Huddleston (84-1270

3/15/84 *ROA.F.* Record on appeal filed, (Supplemental Certified List), Orig. only.

3/26/84 NAPR.F. Notice of appearance filed by Ashton, attorney for appellee

3/29/84 M.CON.F. Petitioner's motion to consolidate filed, orig & 3cc, c/s moot-see order of March 28, 1984.

4/3/84 HRG.SET MAY., '84 TERM, DENVER

4/5/34 NAPR.F. Notice of appearance filed by Blount, Jernigan & Arnold as attys. for appellant. (84-1407)

*4/9/84 BR.F Appellant's brief filed, orig and 10cc, c/s.

NAPR.F Notice of appearance filed by Ashton as attorney for respondent in No. 84-1407.

*4/6/84 NAPR.F. Notice of appearance filed by Ashton as attorney for responden

4/18/84 M.F.BR. Motion to file brief filed.

M.F.BR.DISP. Petitioner's motion to file brief filed, (orig. & 13 cc,c/s, granted to file, RLH, parties notified by mail.

BR.F. Petitioner's brief filed, orig. & 13cc. c/s.

ADD.AUTH.F. Petitioner's additional authority filed, orig. & 25 cc. c/s

4/19/84 ADD. AUTH. F. Petitioner's additional authority filed, orig. & 9 cc.c/s. for 84-1011

ADD. AUTH. F. Intervenors American Financial Services and Household Finance additional authority filed, orig. & 9cc., c/s for 84-1122.

ADD.AUTH.F. Petitioner's additional authority filed, orig. & 9cc, c/s for 84-1122.

4/20/84 *ROA.F.* Record on appeal filed, (Supplemental Certified List) orig.

4/30/84 M.BC. PARTY.F Motion to become a party as amicus curiae filed by Conference of State Bank Supervisors, filed, orig + 9 cc,c/s

*4/30/84 BR.F. (Conference of State Bank Supervisors) Amicus Brief (received but not filed) orig + 9 cc, c/s

5/1/84 BR.F. Respondent's brief filed, orig & 9cc,cs

APX.F. Respondent's appendix filed, orig & 9cc, c/s

5/7/84 BR.F. Petitioner's reply brief filed, orig & 10cc, c/s

5/10/84 BR.F Petitioners' (Dimension, Carroll, Dufek, Mitchell, Shaffer, Shilling, State of Ohil, Ohio Div.

of Svgs. and Loan, Financial Institutions Assurance Corp) reply brief filed, orig. + 9 cc., c/s

5/11/84 BR.F. Petitioners' supplemental reply brief filed, orig and 25cc, c/s (filed in 84-1407)

5/14/85 CS.ARG.SUBM—case argued and submitted—Seth, Doyle, Seymour

9/24/84 OPN.F. Published, signed opinion filed. Seth, Doyle, Seymour Writing Judge is Seth

JM.DISP. Judgment set aside. The Bd shall not attempt to enforce or implemnt such changes herein held invalid.

10/15/84 M.F.ANY.F. Respondent's motion for clarification of opinion filed Orig.

M.STAY.ISS. MDT.F. Respondent's motion to stay mandate until 11/14/84 pending application for cert. 0&3 c/s.

M.STAY.ISS.MDT.RES.F. Petitioners (Dimension Finance) objection to respondent's motion for stay of mandate unti 11/14/84 filed. 0&3 c/s

10/22/84 M.STAY.ISS.MDT.RES.F Petitioner's (Financial Institutions Assur objection to respondent's motion for stay of mandate filed 0&2 c/s

10/25/84 M.STAY.ISS.MDT.RES.F Petitioners' (State of Ohio and Ohio Div. of Savings and Loan Assns.) response in opposition to respondent's motion for stay of mandate filed orig. + 3cc., c/s

10/30/84 OPN.RMK. Opinion correction. Substitute new pages 3 and 4.

11/5/84 M.STAY.ISS.MDT.RES.RPL.F Respondent's reply to petitioner's response to respondent's motion to stay issuance of mandate filed, orig. + 3 cc., c/s

12/18/84 RMK.F. Notification that S.C. has granted extension of time to 1/22/85 to file for cert.

2/14/85 M.STAY.ISS.MDT.DISP. Denied respondent's motion for stay of issuance of mandate. Seth, Doyle, Seymour—parties notified by mail MDT.ISS. Mandate issued to Bd of Governors of Federal Reserve System

2/19/85 P.WRIT.CERT.F. Respondent's (Bd of Governors) petition for writ of cert filed on 2/6/85. S.C. No. 84-1274

2/20/85 OPN.RMK. Opinion correction—substitute new page 22.

2/26/85 MDT. RCPT. F Mandate receipt filed.

5/7/85 P. WRIT.CERT.DISP. Granted respondent's petition for writ of cert. on 4/29/85.

General Docket 84-1011

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

Petition for Review of an Order of the
Board of Governors of the Federal Reserve System

Case No. 84-1011

Consolidated with 83-2696, 84-1122, 84-1257 & 84-1270
For the Procedural Purposes of Record, Briefing,
Argument & Submission.

FIRST BANCORPORATION, PETITIONER,

vs.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, RESPONDENT.

ATTORNEYS FOR APPELLANT:

(A) KENT B. LINEBAUGH
( ) WILLIAM G. MARSDEN
JARDINE, LINEBAUGH, BROWN & DUNN
(A) JOHN D. HAWKE, JR.
(A) LEONARD H. BECKER
( ) JOHN A. KRONSTADT
(A) DOUGLAS L. WALD
ARNOLD & PORTER

1/5/84 CS.DKT. Case docketed; petition for review of a Board order, orig. + 9 cc, c/s.
M.F.ANY.F Petitioner's letter motion suggesting that 84-1011 be submitted to the same panel as case No. 82-1401. Board's order attached. Filed orig. + 9 cc, c/s.

1/24/84 NAPR.F. Notice of appearance filed by Hawke, Becker and Wald as attys for Petitioner

1/31/84 NAPR.F. Notice of appearance filed by Linebaugh as atty. for First Bancorporation, petitioner.

2/20/84 *ROA.F* Record on appeal filed (certified list) orit

2/24/84 M.CON.F.—petitioners' motion to consolidate 83-2696, 84-1011, 84-1122 filed—orig. & 3 cc.—c/s
M.EXP.SCH.O.F.—petitioners' motion to set expedited scheduling order filed—orig. & 3 cc.—c/s (combined with above motion)

* * *ROA.F.* Record on appeal filed, Vols. I-V (pleadings) (1870 pp.) Original (1870 tpp.)

3/5/84 MEMO.IN.SPT.F. Petitioners' memorandum in support of motion to consolidate 84-1011, 84-1122, 83-2696 and to set accelerated briefing and argument schedule/filed, orig. & 3cc, c/s.

**3/1/84 M.CON.RES.F Respondent's response to motion of petitioners in 83-2696, 84-1011 & 84-1122 to consolidate petitions for review filed, Orig. & 3cc., c/s.
M.EXP.SCH.RES.F Respondent's response to petitioner's motion for expedited scheduling filed, Orig. & 3cc., c/s.

3/19/84 M.CON.DISP Granted Petitioner's motion to consolidate cases 84-1011, 84-1122, 83-2696, 84-1257 and 84-1270 disposed of by McKay and Seymour. Parties served by mail.
M.EXP.SCH.O.DISP Granted petitioner's motion to set an accelerated briefing schedule disposed of by McKay & Seymour. Parties served by mail.
O.RMK The petitioners in No. 83-2696 are designated as leading the briefing of this matter for all petitioners disposed of by McKay & Seymour. Parties served by mail.
O.ASGN.CAL Order assigned to Calendar B—Seth. Parties served by mail.
O.BR.DUE Petitioners' lead brief is due 4/9/84. Other petitioners may file statements of joinder and adoption of the lead brief or distinction of their positions in no more than 10 pages each within 10 days thereafter. A joint brief is strongly encouraged. Duplicative arguments will not be favored. Respondent may file a brief of no more than 75

pages within 21 days of service of petitioner's brief. Lead petitioners may file a reply brief within 10 days of service of respondent's brief. Other petitioners may file separate reply briefs of no more than 5 pages each if necessary within 7 days of service of the lead brief disposed of by McKay & Seymour. Parties served by mail. FOR FURTHER DOCKET ENTRIES, SEE CASE NO. 83-2696

General Docket 84-1122

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

Petition for Review of an Order
Of the Board of Governors of the Federal Reserve System

Case No. 84-1122

Consolidated with 83-2696, 84-11011, 84-1257 & 84-1270
for the Procedural Purposes of Record
Briefing, Argument and Submission
COLORADO INDUSTRIAL BANKERS, ASSOCIATION, FORT LUPTON INDUSTRIAL BANK, MONROE INDUSTRIAL BANK, CASTLE ROCK INDUSTRIAL BANK, ARK VALLEY INDUSTRIAL BANK, HOUSEHOLD WELD COUNTY INDUSTRIAL BANK, HOUSEHOLD LAMAR INDUSTRIAL BANK, HOUSEHOLD ALAMOSA INDUSTRIAL BANK, HOUSEHOLD VALLEY INDUSTRIAL BANK, HOUSEHOLD SALIDA INDUSTRIAL BANK, COPPER STATE THRIFT & LOAN COMPANY, AND COPPER STATE FINANCIAL CORPORATION, PETITIONERS,

vs.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, RESPONDENT.

AMERICAN FINANCIAL SERVICES ASSOCIATION,
HOUSEHOLD FINANCE CORPORATION,
(2/16/84 Order) INTERVENORS

ATTORNEYS FOR APPELLANT

(A) LEONARD H. BECKER
(A) JOHN D. HAWKE, JR.
(A) DOUGLAS L. WALD
( ) EDWARD L. WOLF
ARNOLD & PORTER

(A) JAMES J. SANDMAN
ARNOLD & SANDMAN

( ) STEPHEN A. HELLERSTEIN
Hellerstein, Hellerstein & Shore, P.C.

ATTORNEYS FOR APPELLEE

(A) RICHARD M. ASHTON
Assistant General Counsel
Board of Governors of the
Federal Reserve System

INTERVENORS:
( ) John D. Hawke, Jr.
( ) Leonard H. Becker
( ) Douglas L. Wald
( ) Edward L. Wolf
Arnold & Porter

1/27/84 CS.DKT.P.RVW. Case Docketed; Petition for review of an agency order.
M.BC.PARTY.F Motion to intervene filed by American Financial Services Association and Household Finance Corp., orig +3cc,c/s

2/16/84 M.BC.PARTY. DISP—granted motion to intervene filed by American Financial Services Association—McKay, Seymour
M.BC.PARTY.DISP—granted motion to intervene filed by Household Finance Corporation—McKay, Seymour

2/6/84 NAPR.F Notice of appearance filed by Ashton as attorney for Appellee.

2/3/84 NAPR.F. Notice of appearance filed by Sandman as attorney for Appellant

2/3/84 NAPR.F Notice of appearance filed by Hawkw & Becker as attorneys for Appellant.

2/24/84 M.CON.F.—petitioners' motion to consolidate 83-2696, 84-1011, 84-1122 filed —orig. & 3 cc.—c/s
M.EXP.SCH.O.F—petitioners' motion to set expedited scheduling order filed—orig. & 3 cc.—c/s (combined with above motion)

3/1/84 *ROA.F.* Record on appeal filed, Vols. I-V (pleadings) (1870 pp.) Original (1870 pp.)

*3/5/84 MEMO.IN.SPT.F. Petitioners' memorandum in support of motion to consolidate 84-1011, 84-1122, 83-2696 and to set accelerated briefing and argument schedule filed, orig. & 3cc,c/s.

3/1/84 M.CON.RES.F Respondent's response to motion of petitioners in 83-2696, 84-1011 & 84-1122 to consolidate petitions for review filed, Orig. & 3cc., c/s.
M.EXP.SCH.RES.F Respondent's response to petitioner's motion for expedited scheduling filed, Orig. & 3cc.,c/s

3/19/84 M.CON.DISP Granted Petitioner's motion to consolidate cases 84-1011, 84-1122, 83-2696, 84-1257 and 84-1270 disposed of by McKay and Seymour. Parties served by mail.
M.EXP. SCH.O.DISP Granted petitioner's motion to set an accelerated briefing schedule disposed of by McKay & Seymour. Parties served by mail
O.RMK The petitioners in No. 83-2696 are designated as leading the briefing of this matter for all petitioners disposed of by McKay & Seymour. Partes served by mail.
O.ASGN.CAL Order assigned to Calendar B—Seth. Parties served by mail.
O.BR.DUE Petitioners' lead brief is due 4/9/84. Other petitioners bay file statements of joinder and adoption of the lead brief or distinction of their positions in no more than 10 pages each within each 10 days thereafter. A joint brief is strongly encourag Duplicative arguments will not be favored. Respondent may file a brief of no more than 75 pages within 21 days of service of petitioner's brief. Lead petitioners may file a reply brief within 10 days of service of respondent's brief. Other petitioners may file separate reply briefs of no more than 5 pages each if necessary within 7 days of service of the lead brief disposed of by McKay & Seymour. Parties served by mail. FOR FURTHER DOCKET ENTRIES, SEE CASE NO. 83-2696.

General Docket 84-1257

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

Petition to Review an Order of the Board of Governors of the Federal Reserve System

Case No. 84-1257

Transferred from the Sixth Circuit—their no. 84-3089
Related to #84-1270 Consolidated with 83-2696, 84-1011, 84-1122 & 84-1270 for the Procedural Purposes of Record, Briefing, Argument & Submission.

OHIO DEPOSIT GUARANTEE FUND;HORIZON SAVINGS AND LOAN COMPANY; PERMANENT SAVINGS AND LOAN ASSOCIATION; HORIZON SERVICE CORPORATION, PETITIONERS,

vs.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM; PAUL A. VOLCKER; PRESTON MARTIN; NANCY H. TEETERS; HENRY C. WALLICH; J. CHARLES PARTEE; EMMETT J. RICE; LYLE E. GRAMLEY, RESPONDENTS.

ATTORNEYS FOR APPELLANT:
For: Ohio Deposit Guarantee Fund:
( ) PHILIP A. BROWN
( ) ROGER A. YURCHUCK
(A) THOMAS B. RIDGLEY
( ) JOHN J. KULEWICZ
VORYS, SATER, SEYMOUR & PEASE

ATTORNEYS FOR APPELLEE:
(A) RICHARD M. ASHTON
Board of Governors of the Federal Reserve System

1984

1/30	1) Petition to Review an Order of the Board of Governors of the Federal Reserve System (m-no service)
1/30	Certified copy of petition issued to respondent pursuant to Rule 15, FRAP

2/3	2) Motion: petitioner to stay 12/29/84 decision of the Board of Governors of the Federal Reserve System pending appeal (m-2/3)
2/7	3) Order directing oral arguments on the request for stay 2/14/84, declining to issue a stay in the interim, expediting the briefing schedule on the merits for oral argument at the earliest practicable date, and requesting respondents to file a response to the petition for stay by 2/10/84 (Merritt, Kennedy and Wellford, JJ.)
2/10	4) Response: respondents' in opposition to motion for stay (m-2/10) [84-3091]
2/13	5) Reply memorandum of petitioners in support of motion for stay (m-2/13)
2/14	6) Corrected copies of respondents' opposition to motion for stay (m-2/13) [84-3091]
2/14	Cause argued for stay pending review by Ridgley and Harris for petitioners, by Ashton for respondents and case submitted to the Court (Before: Merritt, Kennedy and Wellford, JJ.)
2/16	7) Order denying motion for stay pending review, with instructions (Merritt, Kennedy and Wellford, JJ.)
2/16	8) Letter to parties requesting briefs pursuant to instructions set forth in the 2/16/84 order and extending briefing schedule one week, petitioner's brief to 2/28
2/16	9) Pre-Argument Statement filed on behalf of petitioner.
2/16	10) Appearance of T. Ridgley for the Petitioners.
2/20	11) Memorandum of appellant pursuant to Court's 2/16/84 order (m-2/20)
2/20	12) Memorandum of appellee pursuant to Court's 2/16/84 order (m-2/17)
2/20	13) Appearance of R. Ashton for the Respondent, Board of Governors of the Federal Reserve System.
2/21	13) Order transferring appeals 84-3089 and 84-3091 to U.S.C.A., 10th Cir., and vacating the Court's

expedited briefing schedule of 2/10/84 (Merritt, Kennedy and Wellford, JJ.)

2/21 Certified copy of item 12, contents of office file and copies of the approporiate docket sheets sent to U.S.C.A., 10th Cir.

2/21 Certified copy of item 12 sent to Board of Governors of the Federal Reserve System

2/28/84 CS.DKT.P.RVW. Case docketed. Petition for review. (Transfer from the Sixth Circuit No. 84-3089)

3/1/84 *ROA.F.* Record on appeal filed, Vols. I-V (pleadings) (1870 pp.) Original (1870 tpp.)

3/9/84 NAPR.F. Notice of appearance filed by Ridgley, Yurchuck, Brown & Kulewicz, attys for appellant Ohio Deposit Guarantee Fund.

3/19/84 O.CS.CON. Order cases 84-1011, 84-1122, 83-2696, 84-1257 and 84-1270 consolidated disposed of by McKay & Seymour. Parties served by mai O.RMK For full order and briefing schedule, refer to case 83-2696. FOR FURTHER DOCKET ENTRIES, SEE 83-2696.

General Docket 84-1270

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

Petition to Review an Order of the
Board of Governors Federal Reserve System

Case No. 84-1270

Consolidated with 83-2696, 84-1011, 84-1122 & 84-1257 for the Purpose of Record,
Briefing Argument & Submission. Transferred from the Sixth Circuit—their no. 84-3091 related to #84-1257

STATE OF OHIO; C. LAWRENCE HUDDLESTON, DIRECTOR; OHIO DIVISION OF SAVINGS AND LOAN ASSOCIATIONS, PETITIONERS,

vs.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM; PAUL A. VOLCKER; PRESTON MARTIN; NANCY H. TEETERS; HENRY C. WALLICH; J. CHARLES PARTEE; EMETT J. RICE; LYLE E. GRAMLEY, RESPONDENTS.

ATTORNEYS FOR APPELLANT:

(A) THOMAS B. RIDGLEY
Vorys, Sater, Seymour & Pease

(X) ANTHONY J. CELEBREZZE, JR.
Attorney General

(A) CONNIE J. HARRIS
Assistant Attorney General

ATTORNEYS FOR APPELLEE:

(a) RICHARD M. ASHTON

1984

1/30 1) Petition to Review an Order of the Board of Governors of the Federal Reserve System (m-no service)

1/30 Certified copy of petition issued to respondent pursuant to Rule 15, FRAP

2/3 2) Motion: petitioner for stay Board of Governors of the Federal Reserve System's order of Dec. 29, 1984 pending appeal (m-2/3)

2/7 3) Order directing oral argument on the request for stay 2/14/84, declining to issue a stay in the interim, expediting the briefing schedule on the merits for oral argument at the earliest practicable date, and requesting respondents to file a response to the petition for stay by 2/10/84 (Merritt, Kennedy and Wellford, JJ.)

2/10 4) Response: respondents' in opposition to motion for stay (m-2/10) [84-3089]

2/13 5) Supplemental memorandum (7) of petitioners' in support of motion for stay (m-2/13)

2/14 6) Corrected copies of respondents' opposition to motion for stay (m-2/13) [84-3089]

2/14 Cause argued for stay pending review by Ridgley and Harris for petitioners, by Ashton for respondents and case submitted to the Court (Before: Merritt, Kennedy and Wellford, JJ.)

2/16 7) Order denying motion for stay pending review, with instructions (Merritt, Kennedy and Wellford, JJ.)

2/16 8) Letter to parties requesting briefs pursuant to instructions set forth in the 2/16/84 order and extending briefing schedule 1 week, petitioners' brief due 2/28

2/20 9) Memorandum of appellee's pursuant to Court's 2/16 order (m-2/17)

2/21 10) Letter sent requesting pre-argument statement by 3/2

2/21 11) Memorandum of petitioners on the issue of transfer (m-2/20)

2/21 12) Order transferring appeals 84-3089 and 84-3091 to U.S. Ct. of Appeals for the 10th Cir. and vacating the Court's expedited briefing schedule of 2/10/84 (Merritt, Kennedy and Wellford, JJ.)

2/21 Certified copy of item 12, contents of the office file and copies of the appropriate docket sheets sent to U.S.C.A., 10th Cir.

2/21 Certified copy of item 12 sent to Board of Governors of the Federal Reserve System

2/28/84 CS.DKT.P.RVW. Case docketed. Petition for review. (Transfer from the Sixth Circuit No. 84-3091)

3/1/84 *ROA.F.* Record on appeal filed, Vols. I-V (pleadings) (1870 pp.) Original (1870 tpp.)

3/19 O.CS.CON Order cases 84-1011, 84-1122, 83-2696, 84-1257 and 84-1270 consolidated disposed of by McKay & Seymour. Parties served by mail O.RMK For full order and briefing schedule, refer to case 83-2696. FOR FURTHER DOCKET ENTRIES, SEE 83-2696.

General Docket 84-1407

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

Petition to Review an Order of the
Board of Governors of the Federal Reserve System

Case No. 84-1407

Transferred from the Fourth Circuit—their no. 84-1101
Consolidated with 83-2696, 84-1011, 84-1122, 84-1257, &
84-1270 for the Procedural Purposes of Record, Briefing,
Argument & Submission

FINANCIAL INSTITUTIONS ASSURANCE CORPORATION,
PETITIONER,

vs.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, RESPONDENT.

ATTORNEYS FOR APPELLANT:

(A) JOHN H. ANDERSON
(A) JOHN L. JERNIGAN
(A) R. MARKS ARNOLD
Smith, Anderson, Blount,
Dorset, Mitchell & Jernig

(A) JAMES D. BLOUNT

01-27-84 Case docketed. Awaiting ROA. mh
02-16 DISCLOSURE STMNT. P,N,filed. mh
02-23-84 MOTION (B-142) of P to transfer case to U.S. Court of Appeals for the Tenth Circuit, filed. ses
03-05-84 RESPONSE (B-142) of R to motion to transfer case, filed. ses
03-07-84 Motion (B-142) and response to transfer proceedings transmitted to JDP,*JMS,JDB. (ses)

03-19-84 ORDER granting Rs motion to transfer case to U.S. Court of Appeals for the Tenth Circuit, filed. Copies to Jernigan, Ashton, Mattingly & Tenth Circuit. ses.
3-27 SS.DKT.R.RVW. Case docketed. Petition for review. (Transfer from the Fourth Circuit No. 84-1101)
*PLEADINGS FILED IN EARLIER CASE #83-2696, 84-1011, 84-1122, 84-1257 & 84-1270.
*ROA.F. Record on appeal filed, Vols. I-V (pleadings (1870 pp.) Original (1870 tpp.)
3/28/84 CT.M On the court's own motion, the captioned appeal is ordered consolidated with the appeals in Nos. 83-2696, 84-1011, 84-1122, 84-1257 and 84-1270. Petitioner Financial Institutions Assurance Corporation whall comply with the briefing schedule established in the consolidated cases by order of March 19, 1984, as it pertains to petitioners other than the lead petitioners, disposed of by McKay and Seymour. Parties served by mail.
FOR FURTHER DOCKET ENTRIES, SEE DOCKET NO. 83-2696

BRADFORD NATIONAL CORPORATION
67 BROAD STREET-NEW YORK, N.Y. 10004

Legal Division
Writer's Direct Line

212-530-7880 June 23, 1983

Secretary
Board of Governors of
The Federal Reserve System
Washington, D.C. 20551

Re: Proposed Revision of Regulation Y,
Federal Register Notice—Docket No. R-0470

Gentlemen:

I am writing as counsel to Bradford National Corporation ("BNC") and its related companies, to comment upon certain aspects of the proposed revision of Regulation Y, promulgated under the Bank Holding Company Act of 1956, as amended (the "BHC Act"), which was recently published for comment by the Board of Governors of the Federal Reserve System (the "Board") (hereinafter "the Proposed Regulation").[1] We are specifically concerned with the effect upon BNC of the definition of the term "Commercial loans" added to Regulation Y for the first time by the Proposed Regulation.[2] We strongly believe that if the Board determines to expand the definition of "Commercial loans" for purposes of Section 2(c) of the BHC Act in the manner proposed, that it should also fully grandfather the lending and deposit taking powers of institutions such as BNC's trust company subsidiaries that have relied in good faith upon the Board's and its staff's prior contrary interpretations under the BHC Act and Regulation Y.

Section 2(c) of the BHC Act defines the term "bank" as any institution that both accepts demand deposits and engages in the business of making commercial loans BNC has

[1] Notice of Proposed Rulemaking, 48 Fed. Reg. 23520 (May 25, 1983); comments are due by July 18, 1983.

[2] Proposed Regulation § 225.2(a)(1)(ii). Prior to the Proposed Regulation, Section 225.1(b) of Regulation Y simply adopted the definitions of the BHC Act.

for many years relied upon the fact that its trust company subsidiaries do not engage in the business of making commercial loans as justification for its exemption from the BHC Act, and from any restriction upon their deposit taking powers.

Section 225.2(a)(1)(ii) of the Proposed Regulation defines the term "commercial loans", without qualification, to include "the purchase of commercial paper, certificates of deposit, bankers' acceptances, and similar money market instruments, the extension of broker call loans, the sale of federal funds, and the deposit of interest-bearing funds." The inclusion of these types of money market investments as "commercial loans" is directly contrary to Board and staff rulings pertaining to such companies as Boston Safe Deposit and Trust Company ("Boston Safe") and BNC. It is also inconsistent with the exemption of such "loans" made by nonbank trust companies authorized under Section 4 of the BHC Act by Section 225.4(a)(4) of Regulation Y, and under Section 225.23(b)(3) of the Proposed Regulation.

This construction of the term "commercial loans" was promulgated by the Board in its letter of December 10, 1982 to Mr. William M. Isaac, Chairman, Federal Deposit Insurance Corporation, pertaining to the proposed acquisition by the Dreyfus Corporation of Lincoln State Bank, East Orange, New Jersey (hereinafter the "Dreyfus Interpretation"). In the Dreyfus Interpretation, the Board reaffirmed the broad definition of "commercial loans" for purposes of Section 2(c) of the BHC Act contained in its 1972 decision regarding Boston Safe Deposit and Trust Company ("Boston Safe").[3] As so defined, "commercial loans" included "all loans to an individual, secured or unsecured, other than a loan the proceeds of which are used to acquire property or services used by the borrower for his own personal, family or household purposes, or for charitable purposes." However, as to Boston Safe, the Board further concluded that "commercial loans"

[3] *See*, Letter from Michael A. Greenspan, Assistant Secretary to the Board of Governors of the Federal Reserve System, to Lee J. Aubrey, Federal Reserve Bank of Boston (May 18, 1972). *See also*, Letter from Kenneth A. Kenyon, Deputy Secretary of the Board of Governors of the Federal Reserve System, to Biagio M. Maggiacomo, Greater Providence Deposit Corporation (July 1, 1971).

did *not* include "the purchase of 'money market instruments', such as certificates of deposit, commercial paper, and bank acceptances." The Board also concluded that "the sale of Federal funds by Boston Safe is not tantamount to the making of a commercial loan, for purposes of the Act."

We believe that the justification of the Board's exemption of Boston Safe from the BHC Act, as embodied in subsequent rules and interpretations regarding trust companies by both the Board and its staff, including the exemption previously granted to BNC (through its predecessor—Bradford Computer Systems, Inc.),[4] all as discussed below, continue to fully apply to BNC and its related trust companies. Moreover, we believe that the Dreyful Interpretation reflected the Board's concern with the growing number of "nonbank banks" and was not intended to affect companies such as BNC which had operated under this exemption for some time.[5] We had been reassured by the Board's staff, as well as by staff at the Federal Reserve Bank of New York, that the Board had not decided to apply the Dreyfus Interpretation retroactively. Moreover, Board staff had advised us that the Dreyfus Interpretation was not directed at trust companies operating under this exemption. Accordingly, it appears to us that the Proposed Regulation, absent an express grandfather for BNC and similarly situated companies, goes far beyond the Dreyfus Interpretation and will adversely and unnecessarily affect companies that the Board and its staff had previously held exempt from the BHC Act.

BNC and its related companies have performed the function of offering services in competition with, in many cases, large commercial banking organizations, and have made, we believe, a highly positive contribution to these markets. This was recognized by the Board in its order approving a joint venture between Crocker National Corporation and Western

[4] *See*, Letter from Baldwin B. Tuttle, Deputy General Counsel of the Board of Governors of the Federal Reserve System to Michael A. Greenspan, Esq., counsel to Bradford Computer Systems Inc. (1/26/76), (hereinafter sometimes called the "Tuttle letter").

[5] The Dreyfus Interpretation acknowledges, at page 2: "Between 1970 and 1981, the exemption remained within the narrow confines intended by Congress".

Bradford Trust Company, which concluded that the joint venture would constitute a viable competitive alternative to the large New York banks which dominated corporate trust services provided by bank related organizations.[6] Moreover, as a wholesaler of financial services, including asset management systems and related services, BNC and its related companies offer a means for smaller banking organizations to compete with the large money center bank holding companies as well as unregulated providers of financial services. Continued exemption of BNC from the BHC Act would enable it to continue to perform this valuable function in the marketplace.

BNC and its affiliated trust companies have long provided a range of services to broker/dealers and banks. Bradford Trust Company, New York, New York ("BTC") is a state chartered, Federal Reserve member trust company, that acts as a trustee/custodian for over $40 billion in assets (largely securities). In this capacity, BTC performs functions that parallel the functions of companies such as Boston Safe. However, BTC's functions in this capacity are substantially narrower than those of a traditional trust company. BTC's custody assets are almost entirely managed by banks and other advisors. Except in very limited circumstances, BTC does not have or exercise investment discretion with respect to such assets. Rather, it acts as a physical custodian and recordkeeper. BTC also acts as a named transfer agent or servicer for the named transfer agent for a number of issuers and bank transfer agents, although BTC subcontracts these duties to one or more of its affiliates.

In addition, BTC, through its Clearing Division (formerly Bradford Securities Processing Services, Inc.) is one of the largest independent municipal bond clearing entities. It clears U.S. Government and municipal securities, and offers securities (including equity securities) drafting services. Incident to these clearing activities, BTC extends credit to its broker/dealer customers that clear or draft securities through BTC, which credit is fully collateralized by such securities.

[6] 40 *Fed. Reg.* 1569 (January 8, 1975).

BTC's lending activities have been extensively reviewed by officials and staff at all levels of the Federal Reserve System (BTC has been a member bank since 1977), and were specifically addressed by the Board's Legal Division in the Tuttle letter. In that letter, the Legal Division concluded that, in general, if a trust company such as BTC confined its activities to those specified under the provisions pertaining to nonbank trust companies of the Board's Regulation Y, it would not come within the definition of "bank" in Section 2(c) of the BHC Act. The letter also reaffirmed that BTC's broker call loans would not be deemed to be commercial loans so long as they constituted merely a method of investing a trust company's idle funds and did not constitute a type of revolving business loan, and specifically found that BTC's "sold security transactions" would not cause BTC to be deemed to be engaged in the business of making commercial loans within the meaning of section 2(c).

BTC's (and BTCB's and STC's) clearance related financings fall within the parameters previously set by the Board and its staff, and are also consistent with the regulatory structure established by the Board to govern activities of nonbank trust companies under Section 4 of the BHC Act. Any retrenchment of these activities as to BTC, BTCB and STC would substantially damage their competitive viability. We believe that BTC's role in the securities clearance market, whose participants include major banking organizations, operating through both bank and nonbank subsidiaries, has been highly beneficial. As evidenced by the hiring of BTC's key personnel, our competitors have acknowledged this to be the case.[7] Moreover, inasmuch as the market for these services includes nonbank clearing agencies as well as banks and nonbank trust companies, there seems little danger that the Bradford organization's clearing related financing would serve as a vehicle to evade interstate restrictions on banking.

[7] While BNC has strongly opposed the hiring of its key personnel by Security Pacific Clearing and Services Inc., a nonbanking corporation owned by Security Pacific Corporation, as both unfair competition and as being anticompetitive, it is a mark of BTC's experience and innovative approach to the securities clearance market that it should be so favored by its competitors.

BTC also accepts demand and time deposits incident to its trust activities, as well as demand accounts incident to its clearing functions. Deposits taken in the latter capacity are essentially the same as credit balances accepted by nonbank clearing entities, that have not been treated as "deposits" for purposes of the BHC Act. Indeed, one of our competitors, Security Pacific Clearing and Services, Inc. ("SPCSCI")—a wholly owned nonbank subsidiary of Security Pacific Corporation—has acknowledged holding some $150 million of such customer credit balances. Since SPCSCI takes the position that it may pay interest on these nonreservable credit balances (notwithstanding the prohibition upon payment of interest on deposits contained in Section 225.4(a)(4) of Regulation Y and Section 225.23(b)(3) of the Proposed Regulation), it is becoming a competitive necessity for BTC to be able to offer MMDA deposits (and, when available, Super NOW accounts) to its clearing customers.

Bradford Trust Company of Boston ("BTCB") is a state chartered FDIC insured trust company that provides recordkeeping services for several large mutual fund companies. BTCB has participated in securities clearance loans originated by BTC and has taken demand and time deposits incident to its trust services. In addition, BTCB has accepted All Saver and MMDA deposits that were brokered to it by financial intermediaries.

A third trust company, Security Trust Company of California ("STC") is a state chartered FDIC insured trust company which, by the terms of its charter, is limited to engaging in securities clearance operations similar to those of BTC and providing trust services to IRA, Keogh and other pension plans. Its securities lending and deposit taking activities are essentially the same as those of BTC.

All of BNC's trust company subsidiaries sell, on occasion, Federal funds as an incident to their clearing activities and to utilize idle funds. For example, in the normal course, BTC will not know the full amount of clearing loans that will be required of it by its broker/dealer customers inasmuch as the volume of such loans is directly dependent upon the completion of securities trades cleared during the day. To assure that it has adequate funding for this activity, BTC will pur-

chase Federal funds in the amount that appears necessary and will sell the residue of such funds that remain unused at the end of the day. For lending limit purposes, BTC will participate out any excess amount of its clearance loans. A determination that the sale of Federal funds in this context constitutes the making of commercial loans would therefore have an extremely adverse effect upon BTC's clearing operation. It would be particularly inappropriate since BNC's trust company subsidiaries are "depository institutions" as defined by the Monetary Control Act of 1980, and maintain required reserves under the Board's Regulation D. Thus, no monetary policy purpose would be served by barring these companies from the market for Federal funds. In the ten years or so that BTC has been in existence, moreover, no examiner, or other representative of the Federal Reserve System has ever suggested that BNC would be deemed to be subject to registration under the BHC Act owing to the sale of Federal funds by BTC.

For the reasons stated, we believe it would be appropriate for the Board to fully grandfather BNC and its trust company subsidiaries and other similarly situated trust companies. Such a grandfather should be drafted so as to permit them to continue in the types of "lending" activities in which they have long engaged, with the knowledge of and without objection from the Board. It should also permit them to continue to be free from restrictions on their deposit taking authority.

The Board has recognized that grandfathering may be an appropriate remedy. For example, when Regulation Y was amended to substantially narrow the scope of the Section 4(c)(5) exemption from the nonbank prohibitions of the BHC Act, Section 225.4(e) of Regulation Y was drafted to apply only to acquisitions made after a grandfather date. Given BNC's reliance on longstanding Board and staff interpretations, it appears that this instance is one in which such grandfathering is appropriate.

We would be pleased to offer any assistance you might wish in drafting an appropriate grandfather provision.

Very truly yours,

/S/ Lawrence D. Fruchtman

LAWRENCE D. FRUCHTMAN
Associate Counsel

LDF/lm

cc: Michael Bradfield, General Counsel
Federal Reserve Board

Virgil Mattingly, Associate General Counsel
Federal Reserve Board

Ernest T. Patrikis, Senior Vice President
and Deputy General Counsel
Federal Reserve Bank of New York

FEDERAL RESERVE BANK OF SAN FRANCISCO
San Francisco, California 94120

July 8, 1983

Mr. William W. Wiles
Secretary
Board of Governors of the
Federal Reserve System
Washington, D.C. 20551

Re: Docket R-0470

Dear Mr. Wiles:

* * * * *

225.2(a)(1). This definition is clearly intended to incorporate into the regulation the position that the Board has already taken in the *Beehive* and *Dreyfus* rulings. However, we are not convinced that the Board's expansive reading of "bank" is justified, or that that Congress intended that so-called "nonbank banks" be subject to Board authority under the Bank Holding Company Act.

Furthermore, we note that section 3(e) of the BHC Act requires that every banking subsidiary of the holding company be insured by the FDIC. If the Board and the FDIC definitions of "bank" differ, an institution that comes within the Board's definition but not within the FDIC's definition could not be acquired by a bank holding company. Surely this is not what Congress intended.

* * * * *

COMPTROLLER OF THE CURRENCY
ADMINISTRATOR OF NATIONAL BANKS
Washington, D.C. 20219

July 15, 1983

Mr. William W. Wiles
Secretary, Board of Governors of
The Federal Reserve System
Washington, D.C. 20551

Re: Docket No. R-0470

Dear Mr. Wiles:

* * * * *

EXPANSION OF FRB JURISDICTION

As proposed, revised Regulation Y would redefine commonly accepted banking terms to expand the Board's jurisdiction over transactions subject to its approval. This expansion would primarily be accomplished through the definition of § 225.2 of the revised regulation of the terms "bank," "commercial loans," "demand deposits," and "voting securities."

For purposes of the Bank Holding Company Act, a financial institution is deemed to be a "bank" if it both: "(1) accepts deposits that the depositor has a legal right to withdraw on demand *and* (2) engages in the business of making commercial loans. . . ." 12 U.S.C. § 1841(c) (emphasis added). Neither the BHCA nor the Board's current regulation define the terms used in either part of this two-pronged test. The Board now proposes to define both "demand deposits" and "commercial loans."

The Board proposes to define "demand deposits" in § 225.2(a)(1)(i) as "any deposit with transactional capability that as a matter of practice is payable on demand, and includes deposits accessible by check, draft, negotiable order of withdrawal, or other similar instrument." In our opinion, the proposed definition of demand deposits is unduly broad. In stating this view, the Office offers no comment on the inclusion of NOW accounts in the definition. That issue is likely to be decided in the pending litigation concerning the

Board's Order in First Bancorporation, 68 Fed. Res. Bul. 253 (1982).

However, the Office opposes the newly proposed definition because it is so broad as to apparently include accounts which, unlike NOW accounts, are not even arguably the equivalent of checking accounts. For example, the definition would appear to include the Money Market Deposit Account ("MMDA"). That account provides a transactional capacity that includes up to three checks per month. 12 C.F.R. § 1204.122(e). While depository institutions must reserve the right to require at least seven days' notice prior to withdrawal under 12 C.F.R. § 1204.122(d), checks drawn on the account are, in practice, payable on demand much like negotiable orders of withdrawal. However, unlike the NOW account, the MMDA is not: (1) the functional equivalent of a checking account, (2) advertised as such, or (3) subject to the same reserve requirements as a checking account.

In the First Bancorporation Order the above-enumerated characteristics were strongly relied on by the Board in finding the offering of NOW accounts to meet the first part of the BHCA's two part test of a "bank." The absence of these characteristics makes it clear that the MMDA is in essence a savings account rather than a checking account. At the meeting of the Depository Institutions Deregulation Committee at which the account was authorized, the authority for the MMDA was cited as the Garn-St Germain Depository Institutions Act, of course, rather than the laws authorizing demand deposit or NOW accounts. In discussing whether to allow more than three checks per month to be drawn against the MMDA, the Federal Reserve Board took the position that doing so would be tantamount to treating it as a demand deposit account. Such would be illegal, presumably because of the prohibition against paying interest on demand deposit accounts.

The MMDA was not intended to be considered a demand deposit account for purposes of the BHCA's definition of "bank." The proposed definition of "demand deposits" should be narrowed to exclude accounts such as the MMDA which are not equivalent to checking accounts.

FEDERAL DEPOSIT INSURANCE CORPORATION
Office of the Chairman

July 18, 1983

Honorable William W. Wiles
Secretary of the Board of Governors
of the Federal Reserve System
20th and Constitution Avenue, N.W.
Washington, D.C. 20551

Dear Mr. Wiles:

Subject: *Docket No. R-0470, Proposed Revision to Regulation Y*

We have reviewed the proposed revision to Regulation Y and are deeply concerned over the Board's attempt to resolve by regulation outstanding policy issues that are better left to Congress. The Board is attempting to resolve by regulation serious issues that will affect the entire financial industry. The Board's solution, however, can only serve as a stop-gap measure to a serious problem. As a consequence, we urge the Board to defer action on the proposal. Instead of rulemaking, a wiser alternative is to encourage Congress to immediately undertake a comprehensive review of problems arising from outdated statutory distinctions among banking institutions, thrifts, securities firms, other providers of financial services and commercial firms in general, and to enact permanent legislative solutions to these broad-based problems.

Sincerely,

/S/ Margaret L. Egginton
MARGARET L. EGGINTON
Deputy to the Chairman

UNITED STATES LEAGUE OF
SAVINGS INSTITUTIONS
WASHINGTON OFFICE
1709 New York Avenue, N.W., Washington, D.C. 20006
Tel. (202) 637-8900

July 18, 1983

Mr. William Wiles
Secretary to the Board
Board of Governors of the
Federal Reserve System
Washington, D.C. 20551

RE: Proposed Revision of Regulation Y (Docket No. R-0470)

Dear Mr. Wiles:

The U.S. League of Savings Institutions* wishes to take this opportunity to comment briefly on the proposal by the Board of Governors of the Federal Reserve System to revise its Regulation Y, which implements, *inter alia*, the Bank Holding Company Act of 1956, as amended (BHCA). Apart from the proposed codification in section 225.2(a)(i), (ii) of recent Board reinterpretations of the terms "demand deposit" and "commercial loan", we believe the proposal to be commendable.

Our primary concern with the definitions rests with their potential impact on state-chartered thrift institutions that do not have deposit insurance from the Federal Savings and Loan Insurance Corporation (FSLIC). Many of these institutions, proceeding in a legal environment in which the definitions of demand deposit and commercial loan have been reasonably stable, have become included within holding companies that engage in activities, particularly in the real estate area, that, while authorized under state law, do not comport with the requirements of Regulation Y. Under the Board's proposal, by the mere act of offering NOW accoounts and investing in commercial paper or certificates of deposit, they would find themselves defined, willy-nilly, as bank subsidiaries of bank holding companies, and, presumably, their parents could be forced to stop engaging in nonbanking activities impermissible under Regulation Y. In addition, it appears that proposed section 225.4(c), by its terms, would operate to compel such institutions to obtain deposit insurance from the Federal Deposit Insurance Corporation (FDIC), a task of very uncertain legality under section 3(a) of the Federal Deposit Insurance Act for thrifts not organized as savings banks.

We are confident that the Board does not contemplate precipitating the very substantial disruptions that would accompany a mechanical application of its proposal. While the interpretations upon which the proposed codification is based reflect a clear determination by the Board to apply the BHCA broadly to the activities of companies owning FDIC-insured commercial banks, we detect in them no impulse toward wholesale application of the BHCA and its restrictions to state-chartered thrifts controlled by companies not affiliated with such banks. Indeed, those interpretations show an acceptance of the fact that an institution may engage to some degree in making commercial loans and offering NOW accounts without triggering BHCA coverage.

For instance, in its order in *First Bancorporation*, 68 Federal Reserve Bulletin 253, 254 (March 12, 1982), the Board stated that "[a]lthough savings and loan associations and savings banks ... offer NOW accounts, their lending activities historically have been concentrated in home mortgages and their commercial lending activities are generally quite limited. This and other facts persuade the Board that the activities of such institutions presently authorized by federal statute law generally do not constitute engaging in the business of making commercial loans, and that such institutions

* The U.S. League of Savings Institutions, formerly the U. S. League of Savings Associations, has a membership of 3,500 companies representing over 99% of the assets of the $730 billion savings and loan businesses. League membership includes all types of institutions—federal and state-chartered, stock and mutual. A number of savings banks are also members. The principal officers include: Leonard Shane, Chairman, Huntington Beach, CA; Paul Prior, Vice Chairman, New Castle, IN; William B. O'Connell, President, Chicago, IL; Roy G. Green, Executive Vice President and Washington Director; and Rita Fair, Vice President, Regulatory Operations. League headquarters are at 111 East Wacker Drive, Chicago, IL 60601. The Washington Office is located at 1709 New York Avenue, N.W., Washington, D.C. 20006. Telephone: (202) 637-8900.

are not "banks" for purposes of the [BHCA]." Although the Board in its December 3, 1982 ruling with respect to the Wilshire Oil Company of Texas, 1 Federal Reserve Regulatory Service 4-363.1, stated, in effect, that total exploitation of all the commercial-type lending authorities contained in title III of the Garn-St Germain Depository Institutions Act of 1982 by an institution having neither FSLIC insurance nor a charter from the Federal Home Loan Bank Board would define, as a practical matter, a commercial bank for BHCA purposes, we do not read that document as leading to the conclusion that the Board automatically will define as a bank any state-chartered, non-FSLIC-insured thrift statutorily capable of exercising powers paralleling those extended by title III. In our view, the ruling evidenced, with respect to the Garn-St Germain Act, an attitude favoring a BHCA coverage analysis based on the actual activities of the depository institution in question rather than its hypothetical statutory possibilities. Certainly, the Board's past experience with the applicants in that case and the fact that the subsidiary bank had a huge, existing commercial loan portfolio were central to the Board's determination that voluntary adherence to title III thrift powers would not justify an exemption from BHCA coverage for the depository.

We strongly suggest that, with respect to devising an appropriate test for determining under what circumstnces a state-chartered thrift without FSLIC insurance should fall under BHCA coverage, the Board employ the asset composition standard contained in section 408(n) of the National Housing Act. Section 408(n), enacted by section 335 of the Garn-St Germain Act, essentially states that a unitary savings and loan holding company must observe the activities restrictions applicable to a multiple savings and loan holding company, which are basically the same as those that must be followed by a bank holding company, if its subsidiary FSLIC-insured institution has an asset composition such that the depository fails to qualify as a domestic building and loan association under section 7701(a)(19) of the Internal Revenue Code. As a recently enacted Congressional directive in a directly-related area, we believe the section 408(n) approach has special merit.

With respect to the question of mandating FDIC insurance, we trust that the Board is not proceeding from a determination that all state-chartered thrifts that lack federal deposit insurance and that are in holding company structures must become FDIC-insured if they fall under the Board's expanded definition of the term bank. Such a determination, of course, properly should flow from Congress, not from a regulatory agency. We urge the Board to revise its proposal to remove any question about the ability of these institutions to remain outside the federal deposit insurance system, despite being controlled by other companies, provided they qualify under the aforementioned section 7701(a)(19) test as domestic building and loan associations. The proposal also should stipulate that, if federal deposit insurance is required, it may be obtained from the FSLIC, if otherwise permitted under the National Housing Act, and not just from the FDIC.

As a final matter, we must note that the definitions that are the source of our concern regarding the proposal appear far too aggressive. This is particularly true with respect to the redefining of commercial loan to include the issuance of commercial paper or certificates of deposit, or the deposit of interest-bearing funds. We seriously doubt that this sweeping approach has any real basis in Congressional intent, and suggest that the Board should consider scaling the definition back considerably. Likewise, the definition of demand deposit appears excessively broad. We seriously question, for example, the Board's apparent conclusion that a telephone billpayer account should be equated with a checking account for BHCA purposes. That billpayer accounts may be reserveable under Regulation D does not strike us as relevant, given the specialized concerns underlying the imposition of reserve requirements. As with the proposed definition of commercial loan, we are convinced that the Board's proposal regarding demand deposits has parted company with the intentions of Congress.

To conclude very briefly, the U.S. League is certain that the Board does not intend to disturb arbitrarily current arrangements in that small sector of the thirft industry populated by institutions not statutorily exempted from being defined as banks for BHCA purposes. By adopting the asset

composition test and making the other changes we have suggested, the Board would avoid any unnecessary interference with that sector, without sacrificing any legitimate concerns under the BHCA.

If you have any questions regarding our comments, please do not hesitate to contact us.

/S/ Rita I. Fair
RITA I. FAIR
Vice President
Regulatory Operations

RIF:bbb

KIRKLAND & ELLIS
A Partnership Including Professional Corporations
1776 K Street, N.W.
Washington, D.C. 20006

August 1, 1983

Mr. William W. Wiles
Secretary
Board of Governors of the
Federal Reserve System
20th Street & Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Proposed Revision of Regulation Y Docket No. R-0470

Dear Mr. Wiles:

The undersigned represents the Dimension Financial Corporation, which proposes to purchase the shares of 31 national banks located in 25 states if the Comptroller of the Currency approves pending charter applications. The purpose of this letter is to comment on the Federal Reserve Board's proposed revision of Regulation Y, published on May 25, 1983, 48 Fed. Reg. 23520 (Docket No. R-0470).

The Board's proposed revision purports, pursuant to the Financial Regulation and Simplification Act of 1980, merely to clarify and simplify Regulation Y, 12 C.F.R. Part 225, which implements the Bank Holding Company Act of 1956 as amended ("BHCA"). As part of the revision, however, new definitions that go far beyond clarification and simplification are proposed for the statutory terms "demand deposits" and "commercial loans," which relate to the determination of which financial institutions are "banks" for purposes of the BHCA. Proposed § 225.2(a), 48 Fed. Reg. at 23521, 23538. Under the guise of clarification and simplification, the Board is attempting to amend and expand legislatively the carefully crafted Congressional definition of bank in the BHCA. Such an action would exceed the delegated authority of the Federal Reserve Board.

Each of the proposed definitions is contrary to the plain meaning of the terms as used in the BHCA, as well as to the Congressional purposes underlying the statute. Numerous

previous Board interpretations confirm the invalidity of the proposed definitions. Yet, the Board fails even to attempt to articulate a justification for its radical changes in position, or to make any effort to explicate the rationale for such an expansion of its authority under the BHCA.[1]

I. THE STATUTORY AND HISTORICAL BACKGROUND

Under the BHCA, "bank" is defined as "any institution organized under the law of the United States ... which (1) accepts deposits that the depositor has a legal right to withdraw on demand, and (2) engages in the business of making commercial loans." 12 U.S.C. § 1841(c). The existing Regulation Y defines various terms, including "bank," to have the same meanings as such terms are given in the BHCA. 12 C.F.R. § 225.1. Purportedly relying on its *Beehive* ruling,[2] the Board's proposed revision would define "demand deposits" as "any deposit with transactional capability that is paid on demand as a matter of practice" and explicitly incorporates within that definition "negotiable order of withdrawal" (NOW) accounts. 48 Fed. Reg. at 23521, 23538 (proposed § 225.2(a)(1)(i)). The Board further proposes, by reference to its letter to the FDIC with respect to the Dreyfus Corporation,[3] to define "commercial loans" as "any loan other than a loan to an individual for personal, household,

[1] The Board's Federal Register notice does not even acknowledge that its proposal would constitute a major rewrite of the BHCA. The Notice states that "[t]he Board requests comments on all aspects of the proposed revision of Regulation Y, including definitions of terms," 48 Fed. Reg. at 23520, but does not otherwise provide any information on the definitional changes. The section summarizing the revisions conclusorily and without explanation announces the new definitions, relying solely on references to the Board's Beehive ruling and Dreyfus letter, 48 Fed. Reg. at 23521. Indeed, even the Board's Regulatory Analysis includes not a single word of explanation or justification for, let alone a reasoned analysis of, these drastic definitional changes. *See* "A Regulatory Analysis of Proposals to Revise Regulation Y: 'Bank Holding Companies and Change in Bank Control,'" A-21 (May 1983).

[2] Beehive Financial Corporation, 68 Fed. Res. Bull. 253 (1982) (copy attached as Addendum A).

[3] Letter to William M. Isaac, Chairman of the FDIC, from William W. Wiles, Secretary, Federal Reserve Board (December 10, 1982) (copy attached as Addendum B). *See also* 1 F.R.R.S. 4-363.2.

family or charitable purposes," including such money-market activities as "purchase of commercial paper, certificates of deposit, bankers' acceptances, and similar money market instruments, the extension of broker call loans, the sale of federal funds, and the deposit of interest-bearing funds." 48 Fed. Reg. at 23521, 23538 (proposed § 225.2(a)(1)(ii)).

These proposed definitions conflict directly with the plain meaning of the statutory definition of bank in the BHCA and would effect an unwarranted expansion of the statute beyond the purposes intended by Congress. The BHCA was not intended to grant the Board plenary jurisdiction over inter-state financial institutions. Rather, since its initial passage in 1956, the Act has been intended solely to prevent further concentrations of commercial banking resources and to separate commercial banking and related activities from other commercial enterprises.[4] Twice, in 1966 and again in 1970, Congress narrowed the definition of bank to assure that its scope remained consistent with "[t]he purpose of the Act": *I.e.*, "to restrain undue concentration of control of commercial bank credit, and to prevent abuse by a holding company of its control over this type of credit for the benefit of its nonbanking subsidiaries."[5]

The Board's proposed definitions would exceed these limited purposes and would sweep into the Act's coverage financial institutions not involved in commercial banking, including many institutions previously determined to be outside the Act's reach. Neither the plain words of the statute, the statutory objectives expressed in numerous Congressional pronouncements, nor any rationale heretofore advanced by the Board supports such drastic revisions of the statutory definitions.

[4] S. Rep. No. 1095, 84th Cong., 1st Sess., *reprinted in* [1956] U.S. Code Cong. & Ad. News 2482, 2483.

[5] S. Rep. No. 1179, 89th Cong., 2d Sess. (1966), *reprinted in* [1966] U.S. Code Cong. & Ad. News 2385, 2391. *See* further discussion of the 1966 and 1970 amendments at pp. 9-10, 23-24 *infra*.

II. DEMANDS DEPOSITS AND NOW ACCOUNTS

The Board's attempt to define "demand deposits" to include NOW accounts constitutes an illegal expansion of the statutory term in the BHCA. Important functional differences exist between demand deposits and NOW accounts. Federal legislation, as well as previous Board rulings and actions, have long recognized these differences. And, the Board has advanced no reasoned or substantiated rationale for rejecting its traditional interpretations distinguishing such accounts.

A. NOW Accounts Are Functionally Distinguishable from Demand Deposits.

By attempting to define "demand deposits" to include NOW accounts, the Board obliterates the clear functional distinctions among these different types of transaction accounts. Nowhere in its Notice does the Board recognize these distinctions.

All applicable federal statutes and regulations provide that NOW privileges may be offered only in connection with savings deposit accounts, not demand deposit accounts or deposits payable on demand. NOW accounts offered by member banks (*i.e.*, NOW privileges plus savings deposits) are governed by the Board's regulations applicable to "savings deposit" accounts.[6] NOW accounts, unlike demand deposits, are available only to individuals, sole proprietorships and nonprofit organizations.[7] Federal law authorizes NOW privileges to be offered only in conjunction with interest-bearing

[6] 12 C.F.R. §§ 217.1(e) & 217.5. Under Regulation Q, a member bank may only have three types of mutually exclusive deposits: demand deposits, savings deposits, and time deposits. The same regulation specifically prohibits any member bank from paying interest on a demand deposit. 12 C.F.R. § 217.2(a). The Board's own regulations thus specifically distinguish NOW accounts from demand deposits.

[7] *See* 12 U.S.C. § 1862(a)(2); 12 C.F.R. § 217.1(e)(3). Congress added the demand deposit limitation because it believed that institutions that did not offer demand deposits would not be involved in commercial banking. *See* note 5 *supra* and accompanying text. Since NOW accounts cannot be used by corporations, the availability of such accounts will not generate significant commercial banking business for an institution.

accounts—no interest may be paid on "demand deposit" accounts.[8] A federally insured depository institution has the right to require notice before withdrawal from a NOW account[9]—the same right is not present with respect to demand deposits.

These functional differences between demand deposits and NOW accounts exist today and have been recognized by both Congress and the Board in the past, as described below.

B. Congress Has Consistently Distinguished Between Demand Deposits and NOW Accounts.

Congress has consistently distinguished between demand deposits and NOW accounts. The original 1956 BHCA defined bank broadly to include "any national banking association or any State bank, savings bank, or trust company."[10] But, following two controversial Board decisions holding that an industrial bank would be subject to the BHCA if it "accepts deposits subject to check . . . that are in actual practice, repaid on demand,"[11] Congress added the payable on demand requirement to the BHCA definition of bank. The amended statute thus emphasized through precise statutory language that institutions were banks only if their "depositor has a legal right to withdraw on demand." The Board fully supported this amendment:[12]

[8] 12 U.S.C. § 1832(a)(1).

[9] That this right may not often be exercised does not obviate the significance of its existence. The BHCA defines a "bank" as "any institution . . . which (1) accepts deposits that the depositor has a *legal right* to withdraw on demand." 12 U.S.C. § 1841(c) (emphasis added). The Board's attempt to include within "demand deposits" deposits "paid on demand *as a matter of practice*" thus conflicts squarely with the plain words of the statute. *See* 48 Fed. Reg. at 23521 (emphasis added). Although the *Wilshire* court permitted the Board some latitude to expand the meaning of "demand deposits" beyond the literal words of the statute to reach a sham transaction in a specific circumstance, *see Wilshire Oil Co.* v. *Board of Governors*, 668 F.2d 732, 738 (3d Cir. 1981), *cert. denied*, 102 S.Ct. 2958 (1982), the opinion cannot be read to authorize a general contravention of the statutory requirements.

[10] Act of May 9, 1956, ch. 240, § 2(c), 70 Stat. 133.

[11] Applicability of the Bank Holding Company Act to Industrial Banks, 49 Fed. Res. Bull 165-66 (1963); Industrial Banks as "Banks" under the Bank Holding Company Act, 51 Fed. Res. Bull. 1539-40 (1965).

[12] Hearings on S. 2353, S. 2418, and H.R. 7371 Before a Subcomm. of

> The Board believes that the definition should be amended to cover only "an institution that received deposits payable on demand," thereby limiting coverage to commercial banks (i.e., banks that offer checking accounts), and excluding not only industrial banks but other savings banks that accept funds from the public that are paid on demand. . . . [W]e see no reason in policy to cover such institutions under this act.

Both Congress and the Board thus fully recognized in 1966 the crucial distinction between accounts, such as NOW accounts, that may "in practice [be] repaid on demand" and demand deposits legally required to be "paid" on demand. Both agreed that financial institutions that had the latter type of accounts were banks that should be subject to the BHCA, but institutions with the former type of accounts should not.

Congressional recognition of these distinctions was evident when NOW accounts were initially created. A bill permitting the payment of interest on demand deposit accounts was introduced and rejected in 1979.[13] In its place, Congress enacted the Depository Institutions Deregulation and Monetary Control Act of 1980 ("DIDA"),[14] which permitted NOW accounts. Had Congress viewed NOW accounts as the functional equivalent of paying interest on demand deposits, it could have simply enacted the proposed bill. It did not.

Enactment of the Garn-St. Germain Depository Institutions Act of 1982 evidenced continued Congressional recognition of the difference between NOW accounts and demand deposits.[15] That bill permitted federal savings and loan associations, which already had authority to accept NOW accounts, also to accept "demand accounts," but prohibited payment of interest on such accounts.[16] The Senate Report accompanying the bill underscored the differences between the two types of accounts:[17]

---

the Senate Comm. on Banking & Currency, 89th Cong., 2d Sess. 447 (April 20, 1966, letter of the Board of Governors).

[13] H.R. 3864, 96th Cong., 1st Sess. (1979).

[14] Pub. L. No. 96-221, 94 Stat. 133 (1980).

[15] Pub. L. No. 97-320, 96 Stat. 1469 (October 15, 1982).

[16] Garn-St. Germain Act, § 312 (to be codified at 12 U.S.C. § 1464(b)).

[17] S. Rep. No. 536, 97th Cong., 2d Sess. 15 (1982) (emphasis added).

> Demand accounts may be accepted from persons or organizations that have established a business relationship with the thrift institution; whereas, federal thrifts may now offer *only NOW* accounts . . . the intent of this provision is to permit all federal thrift institutions to offer *checking accounts* to their commercial lending customers. This allows the maintenance of a *demand deposit* even though a business customer with a credit relationship occasionally may not have an outstanding loan.

Congress has carefully distinguished between NOW accounts and demand deposits in legislation dealing with the two types of deposits. Thus, the distinction has been maintained, consistent with the 1966 amendment to the BHCA, between deposits legally required to be paid on demand (demand deposits) and deposits (such as NOW accounts) not legally required to be so paid, even if in practice such accounts are typically paid on demand. Yet, the proposed Regulation Y proposal seeks to obliterate the line between NOW accounts and demand deposits without any discussion by the Board in its Federal Register Notice of this consistent legislative direction.

C. The Board Has Consistently Distinguished NOW Accounts from Demand Deposits.

Consistent with its 1966 position that demand deposits under the BHCA do not include accounts "paid," although not "payable" on demand, the Board and its staff have consistently acknowledged that NOW accounts are not demand deposits. This distinction is clearly set forth by Pauline Heller, former Assistant General Counsel to the Board.[18] Ms. Heller notes that although NOW and other savings accounts "are, as a matter of practice, paid on demand," such deposits "are *not* demand deposits for purposes of the [BHC] Act, because the depository institution is not obliged as a matter of legal right to pay a withdrawal request (or NOW) upon presentation."

---

[18] *Handbook of Federal Bank Holding Company Law* 6-7, n.21 (1976).

The Board honored this distinction as recently as 1981. In the course of rejecting Wilshire Oil Company's attempt to avoid being required to divest the Trust Company of New Jersey (TCNJ) by nominally instituting a notice requirement for demand deposits while simultaneously announcing it did not intend to require notice, the Board noted once again the distinctions between saving deposits with NOW privileges and demand deposits:[19]

> [W]hile Congress had authorized depository institutions to permit withdrawals from *savings accounts* by means of negotiable orders (checks), only individuals and certain not-for-profit organizations may exercise such rights. Pub. L. No. 96-221, § 303, 94 Stat. 146. The Board's regulations provide that any deposit (whether or not interest-bearing) held by a for-profit organization that may be accessed by a negotiable order is not a *savings deposit.* 12 C.F.R. § 217.1(e)(3).... Thus, because TCNJ's transaction accounts are offered to for-profit corporations and other organizations and because TCNJ permits withdrawal from such accounts by negotiable order, the transaction accounts are not "*savings accounts*" under the relevant regulations and are "*demand deposits*" under such regulations.

In its brief to the Third Circuit—which was successful in obtaining affirmance of the Board's decision delcaring Wilshire's TCNJ subsidiary a bank—the Board carefully set forth the basis upon which it had traditionally distinguished NOW accounts from demand deposits. After noting that the FRB and FDIC had traditionally defined demand deposits as deposits that were neither time nor savings deposits, and that Congress had recently permitted individuals and not-for-profit organizations to make withdrawals from interest-bearing savings deposits through NOW accounts, the Board argued to the Court that Wilshire's non-interest-bearing accounts, available to profit-organizations, with an explicitly stated non-binding 14-day withdrawal notice requirement, were demand deposits.[20] The brief further emphasized the

[19] *In re Wilshire Oil Co.*, Fed. Res. Bd. Dkt. No. 1114026, at 14-15 (April 2, 1981) (Final Decision and Order) (emphasis added).

[20] Brief for the Board in No. 81-1560 (June 25, 1981) at 9, 38-41; *see also* Wilshire Oil Co. v. Board of Governors, 668 F.2d 732, 737 n.10 (3d Cir. 1981), *cert. denied*, 102 S. Ct. 2958 (1982), accepting these distinctions.

Board's long-standing view that NOW accounts are not demand deposits even though "financial institutions [with NOW accounts to which advance notice of withdrawal requirements apply] do not normally exercise that right."[21]

Consistent with its long-standing position that NOW accounts are not demand deposits, the Board in several recent instances has permitted bank holding companies to acquire under Section 4(c)(8), as non-bank acquisitions, institutions that both made commercial loans and accepted NOW accounts.[22] With no indication that the lending activities of these institutions fell outside of the meaning of "engaged in the business of making commercial loans," these approvals can only be interpreted as having been predicated on the conclusion that NOW accounts are not demand deposits within the meaning of the BHCA.

The proposed Regulation Y revision of the term "demand deposits" to include NOW accounts thus marks a substantial departure from past, consistent Board positions. Such redefinition goes well beyond any mere "simplification and clarification" of the Board's regulations.

D. The Board Has Advanced No Articulated or Substantiated Basis for Its New Definition of Demand Deposits.

The Board's Federal Register Notice provides no rationale for adoption of its new definition of "demand deposits." To the contrary, the Board merely states that it is "incorporat[ing] Board interpretations of the past," and then cites but one such prior interpretation, its ruling concerning Beehive Financial Corporation. 48 Fed. Reg. at 23521.

[21] *Wilshire* Brief by the Board, *supra* note 20, at 44, n.67.

The Board's position in *Wilshire* reiterated the position it had taken in its earlier brief in United States League of Savings Associations v. Board of Governors, No. 78-2206, U.S. Court of Appeals for the District of Columbia, Brief at 28, 29 n.17:

> The fact that banks might not invoke their right [to demand notice] does not vitiate the distinction between demand and savings deposits, just as it did not in 1913, when Congress statutorily distinguished between these deposits on such basis.

While the Board's views were rejected by the Court, Congress subsequently enacted legislation confirming the prohibition on interest payments on demand deposits that the Board had argued for in this case.

[22] *See, e.g., Heritage Bank*, 66 Fed. Res. Bull. 590 (1980); *First Financial Corporation of New Hampshire*, 66 Fed. Res. Bull. 594 (1980).

As already noted, the Beehive decision marks a 180 degree reversal of past Board decisions. Although the Board claims in that ruling that NOW accounts are demand deposits because the notice requirement is "rarely invoked," and "in practice the customer is permitted to withdraw funds on demand"[23] it had consistently argued to the contrary in the *Wilshire* case and in prior interpretations of the BHCA. Similarly, the Board's claim in Beehive that passage of the DIDA of 1980, which, *inter alia*, subjected NOW accounts to reserve requirements, evidenced a Congressional recognition that NOW accounts should be considered demand deposits, is again belied by its position in Wilshire that demand deposits and NOW accounts were clearly distinguished *in that Act.*[24]

Despite its radical changes in position in the Beehive ruling, the Board put forward not a single word of explanation to justify its departure from established precedent (indeed, its implies no such change has occurred). At best, the only rationale for the new definition can be found in the Board's vague and conclusory claim that there is a "potential for evasion of the Act associated with NOW accounts."[25] What purposes of the BHCA[26] will be evaded in what manner is a question for which the Board proffers no answers, let alone

[23] Beehive Ruling, *supra* note 2, 68 Fed. Res. Bull. at 253.

[24] *Wilshire* Brief, by the Board, *supra* note 20, at 7-8.

[25] Beehive ruling, *supra* note 2, 68 Fed. Res. Bull. at 254.

[26] In *Beehive*, the Board further argued that NOW accounts must be treated as demand deposits so that the Board could, by means of the BHCA enforce reserve requirements against Beehive, which was not federally insured. *See* Beehive Ruling, *supra* note 2, 68 Fed. Res. Bull. at 254-55. The BHCA, however, is concerned with limiting the relationship of banking and commerce, *see* notes 4-5, 12 *supra* and accompanying text. Augmenting Board control over the money supply is not one of its purposes.

In 1980, DIDA extended reserve requirements to any transaction accounts (including NOW accounts) maintained by FDIC-insured banks. Congress thus determined the limits of reserve requirements, and it is clearly improper for the Board to seek to circumvent those limits through the application of the BHCA. Moreover, without any empirical support, it is unreasonable for the Board to assume that the small percentage of uninsured institutions that offer NOW accounts will have any material impact on the money supply.

any evidence that any such practices are threatened anywhere in the United States today. One can only conclude that the Board is relying on the circular reasoning that evasion exists because the Board says it exists. In fact, the absence of any legislative or factual rationale for including NOW accounts as demand deposits suggests to the contrary.

* * * * *

In sum, the Board's attempt through a "clarifying" amendment to expand the definition of demand deposits beyond the clear statutory words of the BHCA and beyond any expressed Congressional intent cannot stand scrutiny. The Board's Federal Register Notice does not even attempt to articulate or substantiate the basis for such expansion of its delegated authority. The proposal to revise Regulation Y to include NOW accounts within the definition of demand deposits should be reconsidered by the Board and rejected.

III. COMMERCIAL LOANS

Just as it has attempted to bootstrap a single unsupported interpretation of "demand deposits" to general regulatory status through its proposed new Regulation Y, the Board proposes to amend the definition of "commercial loan" by reference to a single prior Board statement. The Federal Register Notice again provides no rationale for the new definition, again indicates it is merely "incorporat[ing] Board interpretations," and again cites but one such statement, a letter to the Chairman of the FDIC. 48 Fed. Reg: at 23521. As the FDIC (as well as the Comptroller of the Currency) stated in response to that letter, no such expanded definition of commercial loans can be supported by law or logic. Such expansion would violate the plain words of the BHCA and serve no Congressional purpose expressed in that Act.

A. The Board's Proposed New Definition of Commercial Loans Would Violate Specific Congressional Directions and Conflicts Directly with Numerous Past Board Precedents.

The proposed Regulation Y definition of commercial loans to include within the term, *inter alia*, "commercial paper, certificates of deposit, bankers acceptances, and similar money market instruments," would incorporate the Board's position expressed in its December 10, 1982 letter concern-

ing the Dreyfus Corporation's acquisition of the Lincoln State Bank.[27] The radical departure evidenced by the Board in its proposed new definition of commercial loans has been noted by authorities no less expert than the Federal Deposit Insurance Corporation and the Comptroller of the Currency. Responding to the Board's December 10 letter, the Comptroller termed the Board's position "an abrupt and profound departure from the Board's past interpretations of the BHCA term 'commercial loan.'"[28] The FDIC agreed:[29]

> Heretofore, the Federal Reserve Board's analysis of what constitutes a commercial loan has focused on direct lending activities and has not suggested that the entire spectrum of money market activities and interbank transfer of funds should be incorporated into the concept.

Thus, continued the FDIC, by "dramatically re-cast[ing] the definition of commercial loan," the Board has made a "radical departure from the traditional view of what constitutes a commercial loan [that] raises issues *beyond the scope of regulatory interpretation.*]" Such radical policy changes, concluded the FDIC, "should be brought about by Congressional, *not agency*, action."[30] The FDIC therefore determined not to disapprove the Dreyfus proposal despite the Board's opposition precisely because "the FDIC was constrained to follow the clear legal precedents established over the years."[31]

Those "clear legal precedents" begin with the enactment of the commercial loan limitation itself. Congress added the provision in 1970 to avoid subjecting to the BHCA "institutions which are not in fact engaged in the business of commercial banking in that they do not make commercial

[27] Dreyfus Letter, *supra* note 3.

[28] Comptroller Decision to Charter Dreyfus National Bank & Trust Company, 40 Washington Financial Rep. 308, 310 (1983) (copy attached as Addendum C).

[29] Letter from Margaret L. Egginton, Deputy to the Chairman, FDIC, to William W. Wiles, Secretary, Federal Reserve Board (Dec. 29, 1982) (copy attached as Addendum D).

[30] *Id.* (emphasis added).

[31] *Id.*

loans."[32] Although the narrowing of the definition of "bank" may have been prompted by the case of one trust company, Boston Safe,[33] as the Comptroller has noted, "it is clear that the narrowing ... was not intended to be applicable only to Boston Safe" because "Congress did not intend the exemption ... to be so restrictively interpreted as to subject to the BHCA those financial institutions which need not be subject ... to effect that Act's purpose."[34]

Accordingly, in 1972, the Board determined that Boston Safe was not making "commercial loans" for purposes of the BHCA when it sold federal funds and purchased certificates of deposit, commercial paper, and bank acceptances.[35] A 1981 Board inter-office memorandum noted explicitly that in its Boston Safe decision, "[t]he Board ... concluded that, although commercial in nature, the purchase of federal funds, money market instruments (certificates of deposit, commercial paper, and bankers acceptances) are not considered commercial loans *for the purposes of section 2(c) of the Act*, despite the fact that for other statutory and regulatory purposes these instruments may be considered commercial loans."[36]

[32] S. Rep. No. 1084, 91st Cong., 2d Sess. (1970), *reprinted in* [1970] U.S. Code Cong. & Ad. News 5519, 5541.

The Board argues in its Dreyfus Letter, *supra* note 3, at 2, that the term "commercial loans" was to be "very narrowly applied", based on the tautological statement of the House Managers that "the Board should interpret [this] exemption[ ] as narrowly as possible in order that all bank holding companies which should be covered under the Act in order to protect the public interest will, in fact, be covered." H.R. Rep. No. 1747, 91st Cong., 2d Sess. 23 (1970). The amendment was first offered in the Senate, however, and the quotation in the text above from the Senate Committee Report authoritatively confirms that the only institutions "which should be covered" are those "engaged in the business of commercial banking," as that term has been traditionally used. *See* 116 Cong. Rec. 42422 (1970)

[33] *See* 116 Cong. Rec. 25848 (1970).

[34] Comptroller's Dreyfus decision, *supra* note 28, 40 Washington Financial Rep. at 311.

[35] Letter to Lee J. Aubrey, Vice President, Federal Reserve Bank of Boston, from Michael A. Greenspan, Assistant Secretary, Federal Reserve Board (May 18, 1972) (copy attached as Addendum E).

[36] Office Correspondence of February 10, 1981, at 3 (emphasis in original) (copy attached as Addendum F, released pursuant to an FOIA request to the Board with Board masking as shown).

Since *Boston Safe*, the Board has consistently followed the determination that "commercial loans" as used in the BHCA do not include money market instruments such as broker call loans,[37] or investments in government securities, SBA loans and FHA loans.[38] Recent acquisitions by Gulf & Western, Household Finance Corp., and Citicorp involved institutions that offer NOW accounts and whose financial activities include participation in transactions which would be "commercial loans" under the Regulation Y proposal[39]—yet the Board either approved these acquisitions or took no action to prevent them.[40]

In the Gulf & Western and Household Finance cases, the Board recognized that divestiture of commercial loan portfolios would fully accomplish the BHCA purpose of separating commercial banking from commerce. As the Third Circuit noted in *Wilshire*, the Board's approval of Gulf & Western's

[37] *See, e.g.*, Letter to Michael A. Greenspan from Baldwin B. Tuttle, Deputy General Counsel, Federal Reserve Board (January [illegible] 1976) (unpublished) (broker call loans do not constitute commercial loans) (copy attached as Addendum G).

26

[38] Letter to William N. McDonough, Assistant General Counsel, Federal Reserve Bank of Boston, from Robert E. Mannion, Deputy General Counsel, Federal Reserve Board (November 13, 1980) (unpublished) (investment in government securities, SBA loans, and FHA loans does not constitute "making commercial loans") (copy attached as Addendum H).

It should be noted that because the Board defines "commercial loans" by exclusion ["all loans except . . ."], investments in such obviously noncommercial instruments as government securities arguably come within the definition.

[39] Both Associates National Bank and Valley National Bank—acquired by Gulf & Western and Household Finance, respectively—dealt in Treasury and other government securities and sold federal funds. *See* Bank Administration Institute, *Innerline*, Index of Bank Performance—Individual Bank Profile (1982) (Associates and Valley profiles attached as Addendum I). Although confirmation is not available on the S&L acquired by Citicorp, S&L's routinely engage in money market activities and absent evidence to the contrary, it must be assumed that Citicorp's S&L engaged in such activities. *See* notes 43-44 *infra* and accompanying text.

[40] *See American Banker*, Mar. 13, 1981, at 26 (Gulf & Western) (copy attached as Addendum J); *American Banker*, July 13, 1981, at 1 (HFC) (copy attached as Addendum K); *American Banker*, Sept. 30, 1982, at 4 (Citicorp) (copy attached as Addendum L); *American Banker*, October 4, 1982, at 4 (Citicorp Appendix) (copy attached as Addendum M).

acquisition of Fidelity National Bank, accompanied by divestiture of FNB's commercial loan portfolio, created a situation where "there was no longer the same danger of the abuses related to commercial banking that the BHC Act was designed to prevent."[41]

Indeed, even in the Beehive decision in March 1982, the Board continued to honor its consistent position on the definition of commercial loans. The Board there recognized that savings and loan associations and savings banks (which would accept demand deposits if NOW accounts were included as such) should still not be considered "banks" under the BHCA, as "their commercial lending activities are generally quite limited."[42] Yet, at the time of the decision, a S&L could invest an unlimited percentage of its assets in such instruments as certificates of deposits and other interbank trading vehicles, government securities, and certain types of broker call loans, and could invest up to 20% of its assets in commercial paper[43]—all of which transactions the Board now claims constitute "commercial loans."

Similarly, in the Citicorp case, the Board determined that "a federally insured savings and loan association that offers NOW accounts and *exercises no greater commercial lending powers than are now permitted* to a federal savings and loan association . . . is not a 'bank' for purposes of the BHC Act."[44] Since a S&L's "lending powers" include the unlimited ability to purchase several types of money market and interbank instruments, the Board evidently viewed such activity as not entailing "commercial lending powers."[45] Thus, barely two months before the Dreyfus letter, the Board was still treating the term "commercial loans" as not including such money market activities.

[41] *Wilshire Oil*, 668 F.2d at 739 n.15.

[42] Beehive Ruling, *supra* note 2, 68 Fed. Res. Bull. at 254 n.5.

[43] *See* 12 U.S.C. § 1464(c) (1976) (amended 1982).

[44] Citicorp Ruling, *American Banker*, October 4, 1982, at 14 (emphasis added).

[45] The Board also noted that the acquired S&L had 6% of its assets in commercial real estate loans, but did not mention the value of the S&L's money market activities, thus indicating that such activities were not of concern.

The Board's consistent pattern of decisions followed a course mandated by the plain words of the BHCA. Neither the statute nor its legislative history in any way suggest that the term "commercial loans" was intended to extend beyond its traditional meaning. Moreover, regulation of financial institutions which engage in money market activities for asset/liability management purposes is not necessary under the BHCA, because such institutions pose no threat of concentration of commercial banking resources nor of abuse of commercial banking power through the mixing of banking and commerce. As the Comptroller emphasized:[46]

> [T]here are serious questions as to whether any of the money market activities mentioned in the Board's December 10 letter are commercial loans for purposes of the BHCA. All those money market activities involve only very short term funding commitments by the banks involved. They are an essentially passive medium of investment, are reviewed on a very frequent basis, and do not involve a close lender-borrower relationship. For these reasons, the subject money market activities have little potential of involving the types of commercial lending abuses which Congress wished to prevent through the BHCA.

Stated simply, support for the Board's attempt to reverse its long-standing definition of "commercial loans" cannot be found (and has not been found by either the FDIC or the Comptroller) in the plain words of the BHCA nor implied from the Congressional purposes lying behind the statute.

B. The Board Has Advanced No Articulated or Substantiated Basis for Its New Definition of Commercial Loans.

The Board's abrupt about-face on the meaning of "commercial loans" and its revisionist readings of its previous statements on the subject cannot obscure the incorrectness of interpreting the term to apply to money market activities. Other than unsupported conclusory pronouncements in its referenced December 10, 1982, letter, the Board provides no

[46] Comptroller's Dreyfus decision, *supra* note 28, 40 Washington Financial Rep. at 311.

reason for its new definition of commercial loans in its Federal Register Notice.

The Board's purported rationale—to prevent non-bank banks without commercial loan activities from presenting "a potential for evasion of the purposes of the BHC"—is circular reasoning at best. If such financial institutions were not intended by Congress to be banks subject to the BHCA, there can be no evasion of any Congressional purposes. As noted by the Comptroller,[47] money market and related activities are not commercial loans as that term is normally understood; the Board makes no attempt to demonstrate factually that its regulation of institutions engaged in the former is necessary to prevent abuse of the latter, or even that the two are related in purpose or effect.[48]

The Board attempts to buttress its evasion rationale, again without any factual discussion, by conclusorily announcing that "the proliferation of . . . acquisitions would allow for the expansion of banking across state lines without either state authorization or Congressional approval."[49] The Board's claim at this late date that activities "during the past year"[50] have necessitated drastic revisions of the definition of commercial loans to foreclose the purported evil of insterstate banking severely strains its credibility. To begin with, interstate banking as a general proposition is not prohibited by the BHCA. Indeed, it has flourished for many years under the approval and active encouragement of the Board. The Federal Reserve Bank of Atlanta recently sur-

[47] *See* note 46 *supra* and accompanying text.

[48] Regulation Y itself belies the Board's claimed concerns regarding the possibility of banking and commerce intermingling through money market activities. Section 225.23(b)(3)(iii) permits trust companies to "[make] call loans to securities dealers or purchas[e] money market instruments such as certificates of deposit, commercial paper, government or municipal securities, and bankers acceptances." 48 Fed. Reg. at 23543. These activities, which are termed part of the "traditional activities carried on by trust companies generally," *id.* at 23531, are thus determined to be "nonbanking activities" but are considered a "proper incident" to banking under Section 4(c)(8) of the BHCA. *See id.* at 23530; 12 C.F.R. § 225.4(a)(4) (1983).

[49] Dreyfus Letter, *supra* note 3, at 3.

[50] *Id.* at 3.

veyed the extent of interstate banking activity and concluded simply, "the fact is that banking organizations are providing financial services across state lines and have been doing so for some time."[51] The Atlanta Fed found that "domestic banking organizations control at least 7,383 interstate offices and, if we include interstate offices of foreign banking organizations the total reaches 7,840."[52] As this survey makes clear, interstate banking cannot be considered a new phenomenon justifying radical new definitions of the BHCA.

Indeed, the Board's claim to be concerned with "proliferation" and the "expansion of banking across state lines," conflicts directly with its proposed revision of Regulation Y to permit additional unreviewed expansion. Section 225.25(a)(2) of the proposal would significantly reduce barriers to expansion of existing interstate activities, *see* 48 Fed. Reg. at 23533, 23545, and the Board is even "considering whether to eliminate the requirement for state-by-state approval for *de novo* expansion" across state lines. *Id.* at 23533.

Congress' recent action allowing Federally chartered savings and loans to offer demand deposit accounts and to make conventional commercial loans, while at the same time emphasizing that such expanded-power S&L's are not "banks" under the BHCA further belies the Board's contention that any evasion of the Act would occur absent its new definitions.[53] Congress has recognized that no evasion of the purposes of the BHCA—preclusion of commercial bank concentration and maintenance of the separation of banking and commerce—occurs even when savings and loans engage in both activities that statutorily define banks.[54]

---

[51] Whitehead, Interstate Banking: Taking Inventory, May 1983, *Economic Review*, at 4 (copy attached as Addendum N).

[52] *Id.* at 18. A recent study by Synergistics similarly documents the pervasiveness of interstate banking throughout the United States. *See* Synergistics Research Corporation, *Interstate Banking Directory* (April 1, 1983).

[53] The Garn-St. Germain Depositary Institutions Act of 1982, Pub. L. No. 97-320, §§ 312 and 325 (October, 1982), grants S&L's these expanded powers. *See* S. Rep. No. 536, 97th Cong., 2d Sess. 55 (1982) (such institutions are intended not to be subject to the BHCA).

[54] *See* notes 43-44 *supra* and accompanying text.

Finally, the proposed redefinition of commercial loan would have severe ramifications for existing institutions whose status would be changed from nonbanks to banks. For example, many industrial bank subsidiaries of registered bank holding companies offer NOW accounts and routinely participate in the money markets. The Board approved the acquisition of these institutions as nonbanks under Section 4(c)(8) of the BHCA. Under the expanded definitions of demand deposit and commercial loan now being proposed, these holding company affiliates would have to meet the standards of Section 3 of the Act or be divested. Moreover, state chartered savings banks would also become "banks" subject to the BHCA if Regulation Y is amended as the Board proposes. These banks, of course, have not been subject to regulation by the Board since 1966, and to effect a reversal of the 1966 decision to exclude savings banks—which was supported by the Board[55]—requires an act of Congress, not simply the amendment of a Board regulation.

In sum, as with its attempt to amend the definition of demand deposits, the Board is attempting to expand vastly its definition of commercial loans without even advancing an articulated rationale for or substantial evidence to support such expansion. Such drastic reversal of past Board precedent, inconsistent with both the statutory words and Congressional intent, cannot be justified. The Board should reconsider its proposed redefinition and delete it prior to final promulgation of Regulation Y.

CONCLUSION

The BHCA has the limited purpose of separating commercial banking and commerce, a purpose fully accomplished through interpreting "demand deposits" and "commercial loans" as those terms were intended by Congress and have been traditionally employed by the Board. The Board's abrupt and illogical expansion of those terms can serve no purpose other than administrative aggrandizement. The Board's

---

[55] *See* note 12 *supra* and accompanying text.

proposed definitions cannot be justified by the words of the statute, Congressional intent, or past practice. The Board should not adopt the proposed definitions.

Respectfully submitted,

/S/ Timothy S. Hardy
TIMOTHY S. HARDY
Counsel to Dimension Financial Corporation

ADDENDUM A

First Bancorporation,
Salt Lake City, Utah

Order Conditionally Approving Acquisition of an Industrial Loan Company

First Bancorporation, Salt Lake City, Utah, a bank holding company within the meaning of the Bank Holding Company Act, has applied for the Board's approval under section 4(c)(8) of the act (12 U.S.C. § 1843(c)(8)) and section 225.4(a) of the Board's Regulation Y (12 C.F.R.§ 225.4(a)(2)) to acquire Beehive Financial Corporation ("Beehive Financial") and its wholly-owned subsidiary, Beehive Thrift and Loan Company, Salt Lake City, Utah ("Beehive Thrift"), an industrial loan company. Applicant proposes to engage in lending, industrial loan, leasing, and credit-related insurance activities. These activities have been determined by the Board to be closely related to banking. (12 C.F.R. §§ 225.4(a)(1), (2), (6)(a), and (9)(i)(a)). Industrial loan companies were recently authorized under Utah law to offer NOW accounts, and Applicant also proposes to engage in this activity.

Notice of the application, affording opportunity for interested persons to submit comments has been duly published (46 *Federal Register* 54801). The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 4(c)(8) of the act.

Applicant, the 31st largest banking organization in Utah, controls one bank with total deposits of about $14.7 million, representing less than 0.5 percent of the total deposits in commercial banks in that state, and 0.5 percent of deposits in the Salt Lake City banking market.[1]

Beehive Financial and its subsidiary, Beehive Thrift, have consolidated assets of $3.3 million and liabilities of $2.8 million, including $2.3 million in deposits. In view of the size of the companies involved, the Board concludes that no adverse competitive effects would be associated with this proposal.

Under section 4(c)(8) of the act, the Board is authorized to permit bank holding companies to acquire shares of any com-

---

[1] Banking data are as of June 30, 1980.

pany the activities of which the Board has determined to be "so closely related to banking or managing or controlling banks as to be a proper incident thereto." In determining whether a particular activity is a proper incident to banking or managing or controlling banks, the Board is required to consider whether performance of the activity by a bank holding company can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, or unsound banking practices.

The Board has previously determined that the activity of operating an industrial loan company in the manner authorized by state law is closely related to banking, "so long as the institution does not both accept demand deposits and make commercial loans." (12 C.F.R. § 225.4(a)(2)). An institution engaging in both activities would be regarded as a "bank" for purposes of the act. Section 2(c) of the act defines as a "bank" any institution that "accepts deposits that the depositor has a legal right to withdraw on demand, and engages in the business of making commercial loans." (12 U.S.C. § 1841(c)). The acquisition of a bank in subject to approval under section 3 of the act rather than section 4.

The offering of NOW accounts by an industrial loan company raises a question of whether an institution that offers such accounts and engages in the business of making commercial loans is a "bank" within the meaning of section 2(c) of the Bank Holding Company Act. Institutions that offer NOW accounts generally reserve the right to require 14-30 days' notice before permitting withdrawals from these accounts. The notice requirement is rarely invoked by institutions offering NOW accounts, however, and in practice the customer is permitted to withdraw funds on demand by check or draft. Indeed, for purposes of section 2(c), the Board believes that, until the institution invokes the notice requirement, the depositor has a right to withdraw funds on demand. Moreover, in giving meaning to the demand deposit portion of the definition of "bank", the court in *Wilshire Oil Company of Texas* v. *Board of Governors* (3d Cir. 1981) (filed December 31, 1981), ruled that in using the words "deposits that the depositor has a legal right to withdraw on demand," Congress was concened with the substance rather than the form of the deposit. (Slip Op. at 10-11).[2]

The legislative history of section 2(c) demonstrates that Congress viewed the ability to offer checking accounts as a critical factor in determining whether an institution is a commercial bank. In practice, NOW accounts are advertised as checking accounts and are used as such. Moreover, NOW accounts are regarded as "transaction accounts" under the Depository Institutions Deregulation and Monetary Control Act of 1980 (Pub. Law No. 96-221; 94 Stat. 132) and, whether offered by commercial banks or thrift institutions such as savings and loan associations, are subject to the reserve requirement ratios that apply to demand deposits. (12 U.S.C. § 461). By subjecting NOW accounts to transaction account reserve requirements, Congress recognized that NOW accounts are checking accounts.[3] In view of the function, substance and attributes of NOW accounts, Congress' treatment of NOW accounts, and the potential for evasion of the act associated with NOW accounts,[4] the Board has determined that offering of NOW accounts must be regarded as falling within the first part of the test of whether an institution is a "bank" under section 2(c) of the act.

Accordingly, a nonbanking subsidiary of a bank holding company may not offer NOW accounts and also engage in

---

[2] Similarly, in *First National Bank in Plant City* v. *Dickinson*, 396 U.S. 122, 136 (1968), the Supreme Court held that for purposes of branch banking laws, legal rights between private parties are not necessarily decisive in determining whether a deposit has been created when it is clear that the practical effect of a transaction is the receipt of a deposit.

[3] In authorizing NOW accounts, Congress clearly intended to permit the payment of interest on such accounts, notwithstanding the general prohibition on the payment of interest on demand deposits. However, there is no indication that by authorizing the offering of NOW accounts Congress intended to exempt institutions that provide such accounts from the definition of "bank" in the Bank Holding Company Act.

[4] Because NOW accounts generally perform the same functions as demand deposits, an institution seeking to evade the act might attempt to use such accounts as a substitute for demand deposits. See *Wilshire Oil*, supra.

the business of making commercial loans.[5] Such dual activity is not "closely related to banking" but in fact is banking for purposes of the Bank Holding Company Act. Thus, the Board regards any industrial banking institution that both offers NOW accounts and engages in the business of making commercial loans as a "bank" for purposes of the Bank Holding Company Act.[6] An application to acquire such an institution is subject to approval under section 3 of the act rather than section 4. Thus, the subject application under section 4 of the act may be approved only on the condition that Beehive Thrift will not both offer NOW accounts and engage in the business of making commercial loans.[7]

An industrial bank acquired under section 4 of the act may, however, offer NOW accounts (provided that it also does not engage in the business of making commercial loans) because that activity is closely related to banking since banks in fact offer NOW accounts.[8] Before the Board may permit a bank holding company to engage in a closely related activity, however, the Board must also determine that the activity can reasonably be expected to produce public benefits that outweigh possible adverse effects. The Board is concerned that, unless the NOW accounts offered by Beehive

[5] Although savings and loan associations and savings banks also offer NOW accounts, their lending activities historically have been concentrated in home mortgages and their commercial lending activities are generally quite limited. This and other facts persuade the Board that the activities of such institutions presently authorized by federal statute law generally do not constitute engaging in the business of making commercial loans, and that such institutions are not "banks" for purposes of the act.

[6] Beehive Thrift devotes a substantial portion of its assets to general commercial loans and is engaged in the business of making commercial loans within the meaning of the act.

[7] However, if Beehive Thrift secured FDIC insurance, as is required by section 3(e) of the act, Applicant could acquire Beehive Thrift under section 3 of the act, and Beehive Thrift could both offer NOW accounts and make commercial loans under such circumstances.

[8] The board's previous approvals of bank holding company applications to acquire industrial banking institutions did not authorize the offering of NOW accounts or other types of transaction accounts (such as automatic transfer accounts) by such institutions because those applications did not reference such accounts.

Thrift are subject to interest rate limitations and reserve requirements that apply when such accounts are offered by commercial banks or savings and loan associations, the offering of NOW accounts by an industrial loan company subsidiary of a bank holding company can, and is likely to, undermine the important public policy objectives of the Depository Institutions Deregulation and Monetary Control Act of 1980. In that act, Congress established a policy that all transaction accounts at depository institutions should be subject to interest rate ceilings and reserve requirements.[9]

The Board regards the offering of NOW accounts that are not subject to interest rate ceilings and reserve requirements as an adverse effect within the meaning of § 4(c)(8) of the Bank Holding Company Act, and concludes that it outweighs the public benefits offered by the proposal.[10] Accordingly, the proposal will be approved only if the NOW accounts offered by Applicant are subject to the same federal interest rate limitations and reserve requirements that apply to a federally insured depository institution.

Consummation of the proposal may be expected to result in public benefits in the form of expanded services at Beehive Thrift and, if the proposal is modified as indicated above, would not result in any undue concentration of resources, conflicts of interests, unsound banking practices, or other adverse effects.[11]

[9] The Board believes that the ownership by bank holding companies of industrial loan institutions that offer NOW accounts could undermine the act's objectives by encouraging the growth of transaction deposits at such institutions and diverting deposits away from institutions that are subject to Regulations D and Q.

[10] The Board expressly reserves judgment as to whether more compelling public benefits might be sufficient to outweigh this adverse effect.

[11] In determining that the offering of NOW accounts is a permissible bank holding company activity subject to the conditions specified herein, the Board has taken into consideration the state regulation applicable to industrial loan companies in Utah. The Board notes that Utah law provides for insurance of NOW accounts up to $10,000, establishes minimum capital and reserve requirements for industrial loan companies, and limits the amount of funds that may be loaned to any one borrower. Moreover, the bank commissioner is authorized to monitor the affairs of industrial

Accordingly, based upon the foregoing and all the facts of record, the Board has determined that the balance of public interest factors that the Board is required to consider under section 4(c)(8) if favorable, provided that Applicant complies with the following limitations: Applicant, through Beehive, may not both offer NOW accounts and engage in the business of making commercial loans. If Applicant does not engage in the business of making commercial loans, but does offer NOW accounts, such accounts will be subject to the same interest rate limitations and reserve requirements that would apply to a federally insured depository institution.

Accordingly, the application is hereby approved as conditioned herein. This determination is also subject to the conditions set forth in § 225.4(c) of Regulation Y and to the Board's authority to require such modification or termination of the activites of a holding company or any of its subsidiaries as the Board finds necessary to assure compliance with the provisions and purposes of the act and the Board's regulations and orders issued thereunder, or to prevent evasion thereof.

The activities shall be commenced not later than three months after the effective date of this Order, unless such period is extended for good cause by the Board or by the Federal Reserve Bank of San Francisco, pursuant to delegated authority.

By order of the Board of Governors, effective March 12, 1982.

Voting for this action: Chairman Volcker and Governors Wallich, Partee, Teeters, and Rice. Absent and not voting: Governor Gramley.

(Signed) JAMES MCAFEE,
Associate Secretary of the Board.

[SEAL]

---

loan companies in order to ensure the safety of the deposits accepted by such institutions. The commissioner is also empowered to limit the investments of industrial loan companies, and may issue orders to enforce such determinations.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

December 10, 1982

Mr. William M. Isaac
Chairman
Federal Deposit Insurance Corporation
550 Seventeenth Street, N.W.
Washington, D.C. 20429

Dear Chairman Isaac:

This is in reference to the Notice of Change in Bank Control filed by the Dreyfus Corporation, New York, New York ("Dreyfus"), with the Federal Deposit Insurance Corporation regarding Dreyfus' proposed acquisition of Lincoln State Bank, East Orange, New Jersey ("Lincoln Bank"), a State nonmember insured bank. A copy of the notice was provided to the Board by the New York Regional Office of the Federal Deposit Insurance Corporation for comment.

In its notice, Dreyfus contends that the Bank Holding Company Act (the "BHC Act") is inapplicable to its proposed acquisition of Lincoln Bank on the ground that Lincoln Bank would not be a "bank" under the BHC Act since the bank will, prior to its acquisition by Dreyfus, divest its commercial loan portfolio and thereafter cease to engage in the business of making commercial loans within the meaning of the BHC Act. Dreyfus asserts that this action is sufficient to convert Lincoln Bank from a bank to a nonbank under the BHC Act.

The BHC Act prohibits a bank holding company from engaging in the type of nonbanking activities in which Dreyfus is engaged, and provides that any company that acquires control of a bank must obtain the prior approval of the Board. Section 2(c) of the BHC Act defines the term "bank" as any institution that both accepts demand deposits and "engages in the business of making commercial loans." 12 U.S.C. § 1841(c). By its express terms, the Change in Bank Control Act is not applicable to a transaction that requires

the Board's prior approval under section 3 of the BHC Act. 12 U.S.C. § 1817(j)(16).

In connection with the Board's review of Dreyfus' notice, the Federal Reserve Bank of New York and the Board's staff requested that Dreyfus provide the Board with a detailed description of Dreyfus' proposed plans with respect to Lincoln Bank, particularly with respect to the bank's future lending activities and the extent of the bank's future relationships with Dreyfus and its affiliates. Dreyfus limited its reply to a statement that it planned to assist Lincoln Bank in marketing the bank's deposits to the customers of mutual funds that Dreyfus manages and that it expects to place the bank's funds in certificates of deposit of other banks and similar market instruments "in accordance with sound banking practice and applicable law."

Dreyfus' proposed acquisition of Lincoln Bank is the latest example of a recent trend by nonbanking organizations to acquire commercial banks and to transform such banks into so-called "nonbank banks" by divesting the bank's commercial loan portfolio in an effort to avoid the prohibitions of the BHC Act. The acquisition of such nonbank banks by nonbanking organizations such as Dreyfus is predicated upon an amendment to the definition of "bank" in the BHC Act in 1970. That amendment added to the demand deposit test in the statute the requirement that the institution also be engaged in the business of making commercial loans.

The legislative history of the BHC Act is clear that this amendment was designed for a very limited and special situation involving a single trust company and that the amendment was to be very narrowly applied by the Board.[1] The statement by the House members of the Conference Committee regarding the 1970 Amendments to the BHC Act states that "the Board should interpret [this] exemption[s] as narrowly as possible in order that all bank holding companies which should be covered under the Act in order to

[1] *One-Bank Holding Company Legislation of 1970: Hearings Before the Senate Committee on Banking and Currency*, 91st Cong., 2d Sess., 136-137 (1970).

protect the public interest will, in fact, be covered." H.R. Rep. No. 91-1747, 91st Cong., 2d Sess. 23 (1970).

Between 1970 and 1981, the exemption remained within the narrow confines intended by Congress. In its 1972 decision regarding the Boston Safe Deposit & Trust Company, the Board held that under the BHC Act a commercial loan is any loan other than a loan the proceeds of which are used to acquire property or services used by the borrower for personal, family, household or charitable purposes. The Board, however, stated that the sale of federal funds or the purchase of market instruments such as certificates of deposit, commercial paper, and bankers acceptances would not cause Boston Safe to be regarded as engaged in the business of making commercial loans under the BHC Act in the limited context of the trust company's fiduciary activities. The Board expressly pointed out that its decision was limited to the specific facts of that case. The narrow Boston Safe decision does not and was never intended to exempt from the BHC Act a commercial bank that engages in commercial funding activities of the kind proposed by Dreyfus for Lincoln Bank.

In its 1981 opinion regarding the acquisition by Gulf and Western of Fidelity National Bank, Concord, California, the Board abstained from applying the BHC Act because of assurances that the bank to be acquired would not engage in commercial lending, would limit its loans to individuals for personal, family, household or charitable purposes, and would not be used in any manner to further or enhance the activities of Gulf and Western or its affiliates. The Board did not, however, define or limit the type of loans that are covered as commercial loans under the definition of bank in the Act. In connection with the acquisition by Chrysler Corporation of Automotive Financial Services Inc., an uninsured institution, the only function of which would be to process Chrylser's drafts, the Board expressly stated that the institution may not make commercial loans, including the purchase of commercial paper or bankers acceptances.

During the past year, the Board has noted the large number of acquisitions of "nonbank banks" by nonbanking organizations apparently in reliance on the 1970 amendment to the

definition of bank in the BHC Act and has considered the potential for evasion of the purposes of the BHC Act that are present in the combination of such banking and nonbanking organizations. In particular, the Board is concerned with the difficulty of assuring the enforcement of the prohibition on commercial lending and interrelated activities where the close links associated with common control would be established between the demand deposit-taking function of the "nonbank bank" and commercial lending activities conducted through separate corporate subsidiaries of the parent organization. Moreover, the proliferation of such acquisitions would allow for the expansion of banking across state lines without either state authorization or Congressional approval.

Accordingly, the Board has concluded that the acquisition of nonbank banks has become a vehicle for a substantial evasion and undermining of the BHC Act and that action is necessary to confine the so-called "nonbank bank" exception to the scope originally intended by Congress. To this end, the Board has examined the nature and function of various types of extensions of credit for the purpose of specifying the nature and extent of lending activities that qualify an institution as "engaged in the business of making commercial loans" under the BHC Act. As noted, the Board has consistently held that a commercial loan under the BHC Act is any loan other than a loan the proceeds of which are used to acquire property or services used by the borrower for personal, family, household or charitable purposes. This definition of commercial loan is broad in scope and includes the purchase of such instruments as commercial paper, bankers acceptances, and certificates of deposit, the extension of broker call loans, the sale of federal funds, the deposit of interest bearing funds and similar lending vehicles.[2] These transactions, both in law and in substance, establish a debtor-creditor relationship between business enterprises for purposes that are not personal, family, household, or charitable.

[2] The sale of federal funds and interest bearing deposits were long regarded by the Board as extensions of credit under section 23A of the Federal Reserve Act prior to enactment of the Garn-St Germain Depository Institutions Act of 1982. 96 Stat. 1469.

It is undisputed that Lincoln Bank will continue to accept demand and other transaction deposits and use its deposits to purchase market instruments such as certificates of deposit of other banks.[3] Applying the Board's interpretation of the BHC Act outlined above, it is clear that such activity by an institution that accepts demand deposits and that is chartered and holds itself out as a commercial bank constitutes engaging in the business of making commercial loans within the meaning of the BHC Act and that such an institution is a "bank" under the BHC Act. Thus, the acquisition of control of such a bank by a nonbanking organization such as Dreyfus effects an impermissible commingling of banking and commerce and is prohibited by the BHC Act. In light of the information received regarding Dreyfus' plans for the operations and lending activities of Lincoln Bank, the Board has concluded that Lincoln Bank, after its acquisition by Dreyfus, would continue to accept demand deposits and to be engaged in the business of making commercial loans and that Dreyfus' proposed acquisition of Lincoln Bank is subject to the Board's prior approval under the BHC Act.

Finally, the Board notes that the divestiture plan proposed by Dreyfus for Lincoln Bank's existing commercial loan portfolio, under which the portfolio would be transferred to the Bank of New York, as trustee, until the portfolio could be sold to other banks, is not sufficient to cause Lincoln Bank to cease to be engaged in the business of making commercial loans or to terminate Lincoln Bank's status as a bank under the BHC Act.

For the foregoing reasons, the Board has concluded that Lincoln Bank, a chartered and insured commercial bank, is a bank under the BHC Act and that Dreyfus may not lawfully acquire shares of Lincoln Bank without obtaining the Board's prior approval under section 3(a)(1) of the BHC Act. Accordingly, the Board requests that the FDIC advise Dreyfus that Dreyfus' notice with respect to its proposed acquisition of Lincoln Bank is, as a matter of law, improperly filed under the Change in Bank Control Act because of the

[3] Dreyfus advised the Board that Lincoln Bank will cease making broker call loans and selling federal funds to other financial institutions.

Board's formal determination that the proposed bank acquisiton is subject to section 3 of the Bank Holding Company Act (12 U.S.C. § 1842) and that Dreyfus may not consummate its proposed acquisition in reliance on the Change in Bank Control Act.

While the Board has taken the action described in this letter to limit the 1970 amendment to the definition of bank within the narrow scope intended by Congress, it is clear that it would be desirable for Congress to review the general question of the scope of the definition of bank for the purposes of the BHC Act. Accordingly, the Board intends to request Congress to address this issue at its next session and will submit suggestions for legislative action.

Very truly yours,

/s/ William W. Wiles
WILLIAM W. WILES
Secretary of the Board

cc: Joseph Diamond

COMPTROLLER DECISION TO CHARTER DREYFUS NATIONAL BANK & TRUST COMPANY

This decision relates to the application to charter Dreyfus National Bank & Trust Company which will be located at 600 Madison Avenue, New York, New York.

The Application

The application requests the issuance of a charter to establish the Dreyfus National Bank & Trust Company ("Dreyfus Bank"). Dreyfus Bank initially will concentrate on offering trustee services, custodial services, investment management, and plan administration support to small and midsize employee benefit plans and personal retirement plans. However, it is expected that in the future, Dreyfus Bank will also offer certain deposit certificates and serve as trustee for collective investment funds for pension and profit sharing as well as other institutional investors. As described more fully, *infra*, Dreyfus Bank will not engage in the business of making commercial loans nor will it offer demand deposit accounts.

The Organizers

All of the organizers of Dreyfus Bank are associated with the Dreyfus Corporation ("Dreyfus Corp."), and the new national bank will be a wholly-owned subsidiary of Dreyfus Corp.

Dreyfus Corp. was originally formed as the investment adviser to the Nesbett Fund under the name of John G. Nesbett & Co., Inc. In 1951, a partnership under the name of Dreyfus & Co. acquired the Nesbett Fund and changed its name to The Dreyfus Fund. At that time, Nesbett's investment adviser became subsidary of Dreyfus & Co. and changed its name to Dreyfus Corp. In 1965, Dreyfus & Co. sold to the public 95% of its interest in Dreyfus Corp.

In 1969, The Dreyfus Service Corporation ("Distributor") was organized as a wholly-owned subsidiary of Dreyfus Corp. to serve as underwriter for the distribution of mutual fund shares. Distributor registered as a broker/dealer and became a member of the Philadelphia and Pacific Stock Exchanges.

In 1970, Dreyfus Management, Inc. ("Management") was organized as a subsidiary of Dreyfus Corp. Management serves as investment adviser to various pension funds and other individual accounts. It does not act as investment adviser to any mutual funds.

In addition to the Dreyfus Fund, Dreyfus Corp. also acts as investment adviser to, among others, the Dreyfus Leverage Fund, Dreyfus Number Nine, Dreyfus Third Century, Dreyfus Liquid Assets, Dreyfus Tax Exempt Bond fund, Dreyfus Tax Exempt Money Market Fund, Dreyfus Government Securities Series of Dreyfus Money Market Instruments, and Dreyfus Money Market Fund. These funds, along with other Dreyfus Corp. advised funds, comprise the Dreyfus group of mutual funds.

Dreyfus Corp. also serves as administrator and/or subinvestment adviser of several other money market funds sponsored jointly with independent financial institutions. Dreyfus Corp. currently manages or administers assets of approximately $23.3 billion held by various mutual funds and other investment accounts.

Dreyfus Corp. has also recently acquired Lincoln State Bank, East Orange, New Jersey, subsequent to that bank's divestiture of its commercial loan portfolio.

According to the application, Dreyfus Bank will not have any common officers, directors, or employees with Dreyfus Corp., Distributor, Management, or any of the Dreyfus-advised funds.

The issuance of a bank charter to Dreyfus Bank raises certain issues under the Bank Holding Company Act and the Glass-Steagall Act. The first part of this decison deals with the Bank Holding Company Act issues. The latter part address Glass-Steagall concerns.

I. Bank Holding Company Act Issues

A financial institution qualifies as a "bank" for purposes of the Bank Holding Company Act ("BHCA") if it both "(1) accepts deposits that the depositor has a legal right to withdraw on demand, *and* (2) engages in the business of making commercial loans...." 12 U.S.C. §1841(c)(emphasis added). In its application, Dreyfus Bank has indicated that it will meet neither part of this two-part test. Regarding demand

deposits, the application states that "it is not presently contemplated that the Bank will offer checking account services." Additionally, the application indicates that, at least in the early phases of its operation, Dreyfus Bank will not accept deposits of *any* type. Regarding commercial lending, the application states that Dreyfus Bank will not "engage in the business of making commercial loans."

Although Dreyfus Bank's original application contained the above quoted representations, the Board of Governors of the Federal Reserve System ("Board"), in a December 14, 1982 letter to the Comptroller of the Currency, stated that "the Board considers that [Dreyfus Bank] would be a bank within the meaning of the Bank Holding Company Act...." In making this statement, the Board specifically relied on the reasoning set out in a letter of December 10, 1982, which it sent to the Federal Deposit Insurance Corporation ("FDIC"). That letter concerned the acquisition by Dreyfus Corp. of Lincoln State Bank following that bank's divestiture of its commercial loan portfolio. The December 10 letter stated that, as interpreted by the Board, the BHCA term "commercial loan" included not only traditional commercial loans, but also a wide range of money market activities. The activities specifically mentioned in this regard were "the purchase of such instruments as commercial paper, bankers acceptances and certificates of deposit, the extension of broker call loans, the sale of federal funds, the deposit of interest bearing funds and similar lending vehicles."[1]

---

[1] The FDIC, in a letter of December 29, 1982, to the Board, responded to the Board's letter of December 10. It stated that:

> [T]he Federal Reserve Board has dramatically recast the definition of commercial loan by including within it certain activities that clearly had been excluded from the definition in the past. While we acknowledge the Board's authority to interpret the Bank Holding Company Act, we believe such a radical departure from the traditional view of what constitutes a commercial loan raises issues beyond the scope of regulatory interpretation.

Based on this analysis of the Board's December 10 letter, the FDIC issued a letter to Dreyfus Corp. conveying its intent not to disapprove of the acquisition of Lincoln State Bank. In explaining this action, which was contrary to the course recommended by the Board in its December 10 letter, the FDIC's December 29 letter stated that "the FDIC was constrained to follow the clear legal precedents established over the years...."

The Board's assertion that Dreyfus Bank will be a "bank" under the BHCA is apparently based on the assumption that Dreyfus Bank will both accept demand deposits and engage in one or more of the activities described in the Board's December 10, 1982 letter to the FDIC. By letter of January 14, 1983, Dreyfus Corp. confirmed that, as indicated in its application, Dreyfus Bank does not intend to offer demand deposit accounts. Dreyfus Corp. also indicated that:

> Should [Dreyfus]Bank, in the future, offer time deposits, it is Dreyfus' intention that the Bank would invest the funds derived therefrom (apart from possible investments in personal, family, household or charitable loans) in one or more of the following: certificates of deposit, interest-bearing deposit accounts with other banks, bankers' acceptances, the sale of "federal funds" and government obligations....

Based on the application and Dreyfus Corp.'s January 14, 1983 letter, the Comptroller has concluded that Dreyfus Bank will not be a "bank" for purposes of the BHCA. This conclusion is inescapable in light of the fact that Dreyfus Bank will not accept "deposits that the depositor has a legal right to withdraw on demand"—an activity necessary for qualification as a bank under the BHCA. Therefore, Dreyfus Corp. need not obtain the Board's advance approval in connection with this application.

Because the absence of demand deposit activity is determinative of the question of whether Dreyfus Bank will be a bank under the BHCA, the Comptroller need not determine whether Dreyfus Bank would satisfy the commercial lending test of section 1841(c) through the sale of Federal funds, the making of bank deposits or the purchase of certificates of deposit or bankers' acceptances. However, the Board's December 10 letter commenting on the effect under the BHCA of engaging in these and other money market activities was directed to and considered by the Comptroller in connection with the Dreyfus Bank application. The Comptroller therefore believes it appropriate in deciding the Dreyfus Bank application to offer the following comments regarding the Board's position as expressed in that letter.

A. Past Board Interpretations

The Board's December 10 letter appears to constitute an abrupt and profound departure from the Board's past interpretations of the BHCA term "commercial loan." In determining whether a financial institution will be a "bank" for purposes of the BHCA, those interpretations appear to focus on whether the institution in question has no commercial loan portfolio and has taken steps to ensure that its demand deposit-taking functions will remain separate from the commercial lending activities of its affiliate. *See, e.g.*, the Board's (unpublished) March 11, 1981 letter to Robert C. Zimmer regarding the acquisition by the Gulf and Western Corporation of Fidelity National Bank, Concord, California.

The Board's past interpretations have not indicated that the BHCA term "commercial loan" includes a broad range of money market activities. In fact, the Board has made publicly available a number of interpretations which indicate that the term "commercial loans" does not include certain of the very money market activities which the Board found in its December 10 letter to be included in that term.

For example, an (unpublished) May 18, 1972 letter from the Board to Lee J. Aubrey, Vice President of the Federal Reserve Bank of Boston, stated that Boston Safe Deposit and Trust Company ("Boston Safe") was not making commercial loans for purposes of the BHCA when it sold federal funds and purchased certificates of deposit, commercial paper, and bank acceptances. An (unpublished) January 26, 1976 letter to Michael A. Greenspan from Baldwin B. Tuttle, the Board's Deputy General Counsel, stated that a trust company operating under the Board's Regulation Y[2] would not be engaged in the business of making commercial loans for purposes of the BHCA when it made broker call loans. The letter also noted that, under Regulation Y, nonbank trust companies may engage in the "purchase of money market instruments such as certificates of deposit, commercial paper ... and banker's acceptances."[3] and that these activi-

[2] 12 C.F.R. §225.

[3] 12 C.F.R. §225.4(a)(4)(iii).

ties will not bring the subject financial institutions within the BHCA definition of "bank." In a May 28, 1981 letter to Chrysler Corporation (Fed. Banking L. Rep. (CCH) ¶ 98,770), the Board stated that a state-chartered bank to be owned by a Chrysler Corporation subsidiary would not be a "bank" for purposes of the BHCA by virtue of "the purchase of United States government and agency obligations, certificates of deposit and time deposits, and repurchase agreements of financial institutions with respect thereto . . . ." Notably, this letter states that, in contrast, Chrysler's nonbank bank should not invest in commercial paper and bankers' acceptances since those instruments "could substitute for commercial loans." However, even this cautioning statement regarding two specific money market investments does not appear to be fully consistent with the Board's December 10 letter to the FDIC. The statement that the two investments could *substitute for* commercial loans appears to indicate that (contrary to the December 10 letter) the two investments are not definitionally include in the BHCA term "commercial loan."

B. The Purpose and Legislative History of the BHCA

The BHCA contains no definition of the term "commercial loan." Nor has the Federal Reserve Board issued regulations defining the term. Because the scope of the term is unclear, its meaning must be determined by reference to the purpose and legislative history of the BHCA. The Comptroller believes that the inclusion of money market transactions within the BHCA term "commercial loans" is not supported by the purpose or the legislative history of the BHCA. Therefore, we are unable to agree with the statement in the Board's December 10 letter that "the acquisition of nonbank banks has become a vehicle for a substantial evasion and undermining of the BHC Act. . . ."

The purpose of the BHCA is "to restrain undue concentration of commercial banking resources and to prevent possible abuses related to the control of commercial credit."[4] The primary commercial banking abuses to be prevented are unsafe

[4] S. Rep. No. 1084, 91st Cong., 2d Sess. (1970) *reprinted in* 1970 U.S. Code Cong. & Admin. News 5519, 5541.

loans to nonbank affiliates, credit allocation practices favoring nonbank affiliates and tying arrangements.[5] In 1970, Congress narrowed the BHCA definition of "bank" in order to exclude financial institutions which accept demand deposits but do not "engage in the business of making commercial loans." In doing so, Congress explained that this change was consistent with the BHCA purpose of preventing the above-described commercial banking abuses. The Senate report stated that:

> [T]he Federal Reserve Board has noted that [the BHCA definition of "bank"] may be too broad and may include institutions which are not in fact engaged in the business of commercial banking in that they do not make commercial loans.[6]

As the Board noted in its December 10 letter, the narrowing of the definition of "bank" was prompted by the case of one trust company, *i.e.*, Boston Safe.[7] As the Board's letter also noted, the exemption created by the narrowing of the definition of "bank" (like a number of other exemptions created by the 1970 legislation) should be interpreted by the Board "as narrowly as possible in order that all bank holding companies which should be covered under the [BHCA] in order to protect the public interest will, in fact, be covered."[8] However, it is clear that the narrowing of the definition of "bank" was not intended to be applicable only to Boston Safe. It is also clear that Congress did not intend the exemption created by that narrowing to be so restrictively interpreted as to subject to the BHCA those financial institutions which need not be subject to the BHCA in order to effect that Act's purpose.

The Comptroller believes that the Board's December 10 definition of commercial loans is not supported by either the general purpose of the BHCA or the specific purpose of the 1970 narrowing of the definition of "bank." As noted, the

[5] *See, e.g.*, 115 Cong. Rec. 32903 (1969) (remarks of Rep. Moorhead).

[6] S. Rep. No. 1084, 91st Cong. 2d Sess. (1970) *reprinted in* 1970 U.S. Code Cong. & Admin. News 5519, 5541.

[7] *See* 116 Cong. Rec. 25848 (1970).

[8] H.R. Rep. No. 91-1747, 91st Cong. 2d Sess. 23 (1970).

specific purpose underlying the narrowing of the definition of "bank" was to exempt entities like Boston Safe which accepted demand deposits but did not engage in the business of making commercial loans. However, as evidenced by the previously noted May 18, 1972, Board letter to Mr. Aubrey, Boston Safe engaged in a number of the various money market activities that the Board's December 10 letter finds to be the making of commercial loans, *i.e.*, the sale of Federal funds and the purchase of certificates of deposit, commercial paper and bankers' acceptances.[9] Thus, if the Board's December 10 interpretation of the commercial loan test is correct, the 1970 amendment would not, of itself, have been sufficient to effect the purpose for which it was intended. The fundamental rules of statutory construction would appear to cast serious doubt on an interpretation of the BHCA which would produce such a result.[10]

The general purposes of the BHCA also appear to provide no support for the Board's December 10 interpretation of commercial loans. These general purposes are discussed in a previously noted January 26, 1976, letter from the Board's Deputy General Counsel to Mr. Greenspan regarding broker call loans. That letter stated that:

> [N]onbank trust companies owned by bank holding companies are permitted to make call loans to securities dealers under section 225.4(a)(4)(iii) of Regulation Y because this type of loan is distinguishable from the ordinary commercial loan in that such call loans are entered into on a daily renewable basis with both parties having the option not to renew, are made primarily as a means of temporarily investing idle funds, and are viewed by the lending institution as an alternative to the purchase of money market instruments, such as commercial paper or bankers' acceptances. This type of "call loan" is thus viewed as a passive medium of investment, with the lender making a daily investment judgment based on its analysis of money market rates. "Call loans" thus

[9] *See also* Moody's Investor Service, Inc., 1972 Moody's Bank and Finance Manual 663-664 (December 31, 1970, Financial Statement of Boston Safe Deposit and Trust Company.

[10] *See* C. Sands, Sutherland Statutory Construction §45.5 (4th ed. 1973).

> do not appear to have the close lender-borrower relationship that is one of the characteristics of commercial loans and which presents the possibility of abuses relating to the control of commercial credit that concerned the Congress in adopting the commercial lending test. Thus to the extent that [the inquiring financial institution] engages in brokers' call loans of this character, the Legal Division believes that such activities would not cause it to be engaged in the business of making commercial loans. [Footnotes omitted.]

For essentially the same reasons cited above, the Comptroller believes that there are serious questions as to whether any of the money market activities mentioned in the Board's December 10 letter are commercial loans for purposes of the BHCA. All those money market activities involve only very short term funding commitments by the banks involved. They are an essentially passive medium of investment, are reviewed on a very frequent basis, and do not involve a close lender-borrower relationship. For these reasons, the subject money market activities have little potential of involving the types of commercial lending abuses which Congress wished to prevent through the BHCA.

Although the legislative history and purpose of the BHCA do not appear to support the Board's December 10 interpretation of the applicability of the BHCA to any of the above-discussed money market activities, this lack of support appears to be even more evident in the case of interbank transfers of funds. As noted previously, the chief commercial lending abuses sought to be prevented by the BHCA are imprudent loans to nonbank affiliates, unfair credit allocation favoring nonbank affiliates, and anticompetiti ying arrangements. These potential abuses are, at most, extremely remote when a bank is engaged in money market activities with other banks, rather than with its nonbank affiliates.

II. Glass-Steagall Act Issues

Because Dreyfus Corp. and its subsidiaries are involved in certain securities activities, the issuance of a national bank charter raises issues under the Glass-Steagall Act. The only applicable portion of the Glass-Steagall Act is section 20, 12

U.S.C. §377. Sections 16, 21, and 32 of the Act are clearly inapplicable.

Section 16 of the Glass-Steagall Act, 12 U.S.C. §24 (Seventh), only restricts certain securities activities of a national bank itself. It contains no restrictions on the securities activities of a national bank's affiliates. The restrictions of section 21 of the Act, 12 U.S.C. §378, have been interpreted similarly by the Supreme Court as applying only to the activities of the bank:

> [T]he language of §21 cannot be read to include within its prohibition separate organizations related by ownership with a bank, which does receive deposits.

Board of Governors v. Investment Company Institute, 450 U.S. 46 58 n. 24 (1981). Thus, sections 16 and 21 are not applicable to the establishment of Dreyfus Bank since the bank itself will not engage in any prohibited securities activities.

Section 32 of the Act, 12 U.S.C. §78, prohibits an individual primarily engaged in certain securities activities from serving as an officer, director, or employee of a member bank. As explained earlier, Dreyfus Bank will have no common officers, directors, or employees with Dreyfus Corp., Distributor, Management, or any of the Dreyfus-advised funds. Accordingly, there is no potential section 32 violation involved.[11]

A. Section 20

The remaining section of Glass-Steagall, section 20, provides that:

> [N]o member bank shall be affiliated in any manner described in subsection (b) of section 221a of this title with any corporation, association, business trust, or other similar organization *engaged principally* in the issue, flotation, underwriting, public sale, or distribution at wholesale or retail or through syndicate participation of stocks, bonds, debentures, notes or other securities. . . .

[11] This is in accord with the Board's December 14, 1982 letter to the Comptroller of the Currency concerning the Dreyfus Bank application. In that letter, the Board concluded that a section 32 violation would occur only "if Dreyfus intends to establish any management interlocks between Dreyfus National and Dreyfus or any of the Dreyfus-managed mutual funds . . . ." Board Letter at p.2.

12 U.S.C. §377 (emphasis added). Dreyfus Bank will be an affiliate of Dreyfus Corp., Distributor, and Management.

The financial data for Dreyfus Corp., its two subsidiaries, and the Dreyfus organization on a consolidated basis for the first nine months of 1982 are set forth below.[12]

	Total Gross Revenues	Total Sec. 20 Revenues	Sec. 32 Revenues as % of Total Gross Revenue
Dreyfus Corp.	$75,957,000	-0-	0%
Distributor	539,000	310,000	58%
Management	3,820,000	367,000	0%
Consolidated	$80,316,000	$310,000	0.004%

Dreyfus Corp. itself is engaged in no section 20 activities. Thus, its proposed affiliation with Dreyfus Bank poses no section 20 problem. Management also is engaged in no section 20 activities. Accordingly, the proposed affiliation between Management and Dreyfus Bank also poses no section 20 problem.

While revenues from Distributor's section 20 activities constitute less than one-half of one percent of the consolidated revenues of Dreyfus Corp. and its subsidiaries, they constitute 58% of the total revenues of Distributor. Thus, if Distributor were considered alone, it would be an impermissible affiliate of Dreyfus Bank because it is "engaged principally" in section 20 activities.

To determine whether an entity is "engaged principally" in section 20 activities, it is appropriate to refer to the Supreme Court's decision in *Board of Governors v. Agnew*, 329 U.S. 441 (1947).

That decision was an interpretation of the "primarily engaged" language of section 32. However, in the course of its opinion the Court analyzed the interrelationship of "en-

[12] The dollar amounts and percentages of section 20 revenues for Dreyfus Corp., Distributor, and Management are substantially similar for the year ended 1981. For the sake of simplicity, the section 20 analysis need only employ the most recent figures.

gaged" (section 21), "primarily engaged" (section 32) and "engaged principally" (section 20) as those terms are used in Glass-Steagall, making clear that the degree of business necessary to be "engaged principally" in an activity is greater than the degree of business necessary to be "primarily engaged" in an activity. 329 U.S. at 446-448.

A firm that receives less than 10% of its gross income from section 32 business is clearly not "primarily engaged" in such business.[13] Under the "single entity" theory, as explained below, Distributor must be considered as part of the total Dreyfus enterprise for section 20 purposes. The resulting consolidated entity derives less than one-half of one percent of total revenues—$310,000 for the first nine months of 1982—from section 20 activities. Since these consolidated figures do not approach the level required to satisfy the "primarily engaged" test of section 32, they obviously cannot violate the less stringent section 20 test of "engaged principally."

B. "Single Entity" Theory

The "single entity" theory disregards, under appropriate circumstances, the separate corporate existence of a subsidiary engaged in section 20 activities in determining whether a corporate group affiliated with a member bank is, as a whole, "principally engaged" in section 20 activities. The Comptroller has previously found the theory to be a valid analytical technique. Where a subsidiary is wholly-owned and acts as a servicing or selling arm in connection with the activities of the parent, the theory is particularly pertinent. To hold otherwise would needlessly require corporations wishing to avoid section 20 violations to dissolve separate subsidiaries engaged in section 20 activities and to assume

[13] Decision of the Comptroller of the Currency on the Application to Charter J. & W. Seligman Trust Co., N.A., February 1, 1983, at p. 9, n. 5. Previous Board opinions have also suggested that a firm receiving more than $10 million in gross income from section 32 business is "primarily engaged" in such business. This figure has not been adjusted for inflation and was not mentioned in the Board staff's December 14, 1981 opinion. Staff Opinion 3-939, *Federal Reserve Regulatory Service*, Vol. 1, pp. 389-390.

those responsibilities directly, even though there are many legitimate business reasons explaining and justifying separate incorporation.[14]

The Supreme Court has indicated that the single entity theory is an appropriate technique for analyzing affiliations and management interlocks in the context of the relevant Glass-Steagall Act provisions. As pointed out in the Comptroller's decision to charter J. & W. Seligman Trust Company, N.A.,[15] the Court endorsed this approach in a section 32 context in *Investment Company Institute v. Camp*, 401 U.S. 617, 626 & n.12 (1971). Moreover, by rejecting the theory as a means of interpreting the absolute prohibitions in section 16 and 21, the Court in a 1981 decision implicitly endorsed its use for the "less stringent standard" in section 20.[16] As our earlier decision also noted, the Board has repeatedly used the theory to analyze section 32 violations and, in at least one instance, to determine the absence of a section 20 violation.

The Comptroller finds the single entity theory to be applicable here because Distributor performs only activities which could be performed by Dreyfus Corp. itself (and would, if so performed, obviate any section 20 problems because of the small amount of section 30 activities vis-a-vis other activities), and because Distributor's activities are performed solely on behalf of Dreyfus Corp. in connection with its sponsorship of a family of investment companies which it advises. Furthermore, the principal reason for Distributor's incorporation as a separate subsidiary was to take advantage of lower net capital requirements under the Securities Exchange Act of 1934. This is a legitimate business reason for using the subsidiary approach and as such should not have

[14] Among the legitimate business reasons is a desire to minimize liability, ease the impact of regulation and taxation, and provide a large number of executive positions in an organization. The latter consideration can be a useful marketing tool, since some potential customers may prefer to deal with the "president" or a subsidiary rather than with an "assistant vice president" of a corporation without subsidiaries.

[15] *See* note 13, *supra*.

[16] *Board of Governors v. Investment Company Institute*, 450 U.S. 46, 58-59 n.24 and n.26 (1981).

any effect on the Glass-Steagall analysis. Accordingly, the proposed charter would not violate section 20.

C. The Dreyfus-Advised Funds

The Comptroller has determined that Dreyfus Bank would not be "affiliated," as that term is defined in 12 U.S.C. §221a(b), with any of the Dreyfus group of mutual funds,[17] and therefore would not be in violation of section 20 of Glass-Steagall. Subsections (1), (3), and (4) of section 221a(b) are clearly inapplicable here, Dreyfus Bank will not own a majority of the voting shares of any advised fund. None of the directors of any advised fund will be directors of Dreyfus Bank. An advised fund will not own or control, directly or indirectly, a majority of the shares of Dreyfus Bank, or more than 50% of the number of shares voted for election of the directors of Dreyfus Bank, or control in any manner the election of a majority of the directors of Dreyfus Bank. Therefore, the sole question is whether, under the meaning of subsection (2), the parent of Dreyfus Bank (*i.e.*, Dreyfus Corp.) controls "through stock ownership or in any other manner" the advised funds. Since the percentage ownership by Dreyfus Corp. and its subsidiaries of any of the shares of the advised funds is minimal,[18] the question becomes whether Dreyfus Corp. "controls" those funds "in any other manner."

The specific types of affiliations identified in Section 221a(b) all relate to control of companies at the level of equity ownership or board selection or control. They do not cover control of day-to-day management in situations where that is not coupled with the sort of policy control exerted by a board of directors or a shareholder acting through the

[17] This determination is important since an open-ended fund is apparently regarded by the Board as "engaged principally in the issue" of securities. Board letter, *supra* n. 11, at p. 2.

[18] At September 30, 1982, Dreyfus Corp. had investments of $51,012,000 in the shares of four advised mutual funds. In no instance did the percentage investment in any fund exceed 1%. These funds represented working capital of Dreyfus Corp. placed on a temporary basis, and as such may fluctuate daily. Additionally, at September 30, 1982, Dreyfus Corp. had invested a total of $540,000 as initial paid-in capital for purposes of initiating sixteen new mutual funds at such date. These investments represented the required "seed money" for purposes of organizing such mutual funds.

elected board. In our view, the more general reference to "control . . . in any other manner" in § 221a(b)(2) is intended to cover only control that relates to the same sort of policy level control covered by the numerous specific types of control specified in § 221a(b) and not the managerial authority vested in corporate officers or contractual managers such as investment advisers.

Such an interpretation is in accord with the *ejusdem generis* doctrine of statutory construction. Under this rule, where specific words of definition (*e.g.*, control through majority share ownership or election of directors) are used in a statute along with general words of definition (*e.g.*, control in any other manner), the general words must be construed to encompass only situations similar in nature to those enumerated in the specific words.[19] If the general definitional words were to be given their most expansive meaning, they would obviously include those situations designated by the more specific definitional words, making the specific words superfluous. Accordingly, the phrase "control . . . in any other manner", as used in section 221(b), should only include types of control similar in nature and effect to majority shareholding or the election of directors, *i.e.*, the ability to control policy.

The issue arises as to whether a mutual fund's investment adviser "controls" that fund for Glass-Steagall purposes. The Comptroller, who has ample authority to interpret the Glass-Steagall Act,[20] has determined that the Investment Company Act of 1940 ("the Act") confers so much authority on

[19] *See* C. Sands, Sutherland Statutory Construction § 47.17 (4th ed. 1973).

[20] *See, e.g.*, OCC opinions on bank proposals to offer discount brokerage services, CCH Fed. Banking L. Rep. ¶ 99,284; to issue mortgage-backed pass-through securities, CCH [1973-1978 Transfer Binder] Fed. Banking L. Rep. ¶ 97,093; to offer bank automatic investment services, CCH [1973-1978 Transfer Binder] Fed. Banking L. Rep. ¶ 96,272, upheld on the merits in *New York Stock Exchange* v. *Smith*, 404 F. Supp. 1091 (D.D.C. 1975), *vacated on ripeness grounds*, 562 F.2d 736 (D.C. Cir.), *cert. denied*, 435 U.S. 942 (1978). Numerous staff opinions, published and unpublished, have been issued over the years; *see, e.g.*, "OCC Staff Analysis of Certain Legal Issues Raised by Retail Repurchase Agreements" at 5 (accompanying Banking Circular 157 dated May 13, 1981), 5 CCH Fed. Banking L. Rep ¶ 60,798.35 at 38,857.

the disinterested members of a fund's board that control, as the term is used in section 221a(b), of a fund by its investment adviser appears to be precluded, especially where, as here, each fund's board is comprised of a majority of disinterested directors. The Comptroller reached a similar conclusion in the February 1, 1983 decision approving the charter of J. & W. Seligman Trust Company, N.A.[21] Because that recent decision contains an in-depth discussion of the Act and its protective features,[22] the analysis need not be repeated here. It should be sufficient to note that the Comptroller's conclusion in the J. &W. Seligman decision was that the operations of mutual funds are directed by the fund's directors, not by the fund's advisers or managers. At least 40% of the directors of a fund must be disinterested persons, to whom the Act assigns especially sensitive tasks, including what the Supreme Court describes as the "critical functions" of approving the advisory contracts and selecting the accountants.[23] In short, even in a situation where only 40% of a fund's directors are disinterested persons, the Act can be regarded as a statutorily mandated system for independent directorial governance of investment companies, a system which negates control by the adviser.[24] The specific issue of the role of the independent directors of a Dreyfus-advised mutual fund (Dreyfus Liquid Assets) has been considered in a recent court decision. In *Krasner v. Dreyfus Corp.*, 90 F.R.D. 665 (S.D.N.Y. 1981), a case involving the reasonableness of the investment advisory fee charged by the investment adviser (*i.e.*, Dreyfus Corp.), the court noted that:

[21] *See* note 13, *supra*.

[22] Decision of the Comptroller, *supra* n. 13, at 16-22.

[23] *Burks v. Lasker*, 441 U.S. 471, 485 n. 15 (1979). It should be noted that the Act also gives the directors special termination rights over the advisory contract. Specifically, the contract must provide "that it may be terminated at any time, without the payment of any penalty, by the board of directors . . . on not more than sixty day's written notice to the investment adviser." 15 U.S.C. §80a-15(a)(3). Moreover, the Act's legislative history makes clear that Congress intended the directors to have a fiduciary duty with respect to "all of the affairs of the fund." S. Rep. No. 184, 91st Cong., 1st Sess. at 6 (1969).

[24] Decision of the Comptroller, *supra* n. 13, at 21-22.

> Section 15(c) of the Act further requires the directors of a fund to request and evaluate the same type of information that the Adviser is obligated to provide. The Court is satisfied that the directors, all of whom are reputable people in business and the professions, have done just that. In addition, under section 15(c), a management agreement can only be approved by a majority of non-interested directors appearing in person at a special meeting called for that purpose. As noted previously, this requirement was met in this case.
>
> The board meetings held to approve the management agreement were conducted in the following manner. Each meeting was attended by both the Fund's independent counsel, who advised the non-interested directors of their fiduciary obligations, and personnel from Dreyfus, who provided information and answered questions. When the non-interested directors were satisfied that they had received sufficient information, the Dreyfus personnel left the meeting, and the non-interested directors continued their discussions in private, with their attorney present. At each such meeting, the management agreement was approved unanimously by the non-interested directors. In short, the deliberations of the directors were a matter of substance rather than a mere formality.

Id. at 671, 672.

According to correspondence received from Dreyfus Corp., a majority of the Directors of *each* Dreyfus-advised mutual fund are disinterested directors as that term is defined in the Act. At each Board of Director's meeting, the directors, a majority of whom are disinterested, review in detail the fund's investment portfolio. In addition, the directors review the financial operations as well as legal, operational and other significant matters. The directors conduct these reviews with representatives of the investment adviser who respond in detail to questions posed by the directors and independent counsel who represent the fund and its independent counsel who represent the fund and its independent directors. The directors are further provided with detailed information so that they can review the services rendered by the investment adviser during the preceding year.

The Board appears to have recently taken the view that an organization which sponsors, organizes or manages a fund also "controls" it for purposes of section 20.[25] It has also recently suggested that correct use of the single entity theory in this context requires the inclusion in the consolidated Dreyfus enterprise of the investment companies or funds for which Dreyfus Corp. serves as investment adviser.[26] Normally, the Comptroller would give great deference to the Board's views. However, for the reasons stated above, we are unable to do so here. Moreover, the Board's views represent a departure from past Board precedents and do not appear to be legally supportable.[27] In fact, the Supreme Court, in *Board of Governors v. Investment Company Institute*, 450 U.S. 46, 50-51 (1981), specifically recognized that investment advisers of investment companies typically manage the Company's business. Nevertheless, the Court upheld a ruling of the Board that bank affiliates could serve as investment advisers at least if they did not "organize, sponsor, or control" the investment companies.

In addition to the lack of any management control, there is also a lack of any control through share ownership. In no instance does aggregate share ownership of any fund by all Dreyfus Corp. officers and directors as a group exceed 1% of outstanding shares. With respect to ownership of Dreyfus Corp., there are no individuals who can be viewed as controlling stockholders. Share ownership is widely dispersed and traded on the New York Stock Exchange. The largest single stockholding that of the Chairman of the Board, President, and Chief-Executive Officer of Dreyfus Corp., amounts to less than 6% of Dreyfus Corp.'s outstanding shares.

Accordingly, both as a matter of law and of fact, Dreyfus Corp. does not "control" the funds it advises within the meaning of 12 U.S.C. §221a(b)(2). The provisions of the Investment Company Act, the particular characteristics of Dreyfus Corp. and of the advised funds, and the absence of any controlling shareholders establishes the lack of any section 221a(b) affiliation between Dreyfus Corp. and those funds. Accordingly, the issuance of a charter for a national bank, the stock of which is to be owned by Dreyfus Corp. will not cause a violation of section 20.

[25] Board Letter, *supra* n. 11, at p. 2.

[26] Board Letter, *supra*, n. 11, at p. 3.

[27] *See* 12 C.F.R. §225.125(f) ("In the Board's opinion, the Glass-Steagall Act provisions . . . forbid a bank holding company to sponsor, organize or *control* a mutual fund.") (emphasis added.)

Conclusion

Establishment of Dreyfus Bank will not violate either the Bank Holding Company Act or the Glass-Steagall Act. Furthermore, the Office has determined that the application complies with the provisions of 12 C.F.R. Parts 5 and 9 relating to the organization of a national bank with trust powers.[28] Accordingly, preliminary approval to organize a National Bank with trust powers is hereby granted.

Dated 2/4/83

C.T. Conover
Comptroller of the Currency

[28] Of course, Dreyfus Bank will be subject to all statutory and regulatory provisions applicable to national banks. For example, under 12 U.S.C. §374a, a member bank may not act as agent for any nonbanking entity in making loans to brokers or dealers with securities as collateral. Moreover, the Comptroller has taken the position under 12 C.F.R. Part 9 that it is a breach of trust for a trustee to purchase assets for its fiduciary accounts from or through itself or an affiliate without having specific authority therefor in the appropriate governing instrument, or from an authorized person. Pursuant to this interpretation, the Office has stated that a bank trustee could place transactions through an affiliate only if that affiliate executes those actions at cost and does not make a profit in the process.

FEDERAL DEPOSIT INSURANCE CORPORATION,
Washington, D.C. 20429
Deputy to the Chairman

December 29, 1982

Mr. William W. Wiles
Secretary of the Board of Governors
of the Federal Reserve System
20th & Constitution Avenue, N.W.
Washington, D.C. 20551

Dear Mr. Wiles:

We are writing in response to your letter of December 10, 1982, commenting on the proposed acquisition of Lincoln State Bank by The Dreyfus Corporation ("Dreyfus"). As you know, the Board of Directors of the FDIC has issued a letter to Dreyfus conveying its intent not to disapprove the acquistion of control. It was the conclusion of the FDIC Board that Dreyfus' notice of change of control was properly submitted to the FDIC under the Change in Bank Control Act of 1978, and our Board of Directors was required to respond within the time constraints of the statute.

We have reviewed analogous acquisitions of "nonbank banks" and note that a number of clear precedents exist, dating back a number of years, for a bank to be held exempt from the definition of "bank" in the Bank Holding Company Act based on the divestiture of its commercial loan portfolio prior to the acquisition and its agreement not to engage in the business of making commercial loans in the future. By failing to object previously to that now fairly routine practice, the Federal Reserve Board has, in our judgment, acquiesced in, if not expressly agreed with, a more limited definition of commercial loan on which the public has come to rely.

Heretofore, the Federal Reserve Board's analysis of what constitutes a commercial loan has focused on direct lending activities and has not suggested that the entire spectrum of money market activities and interbank transfers of funds should be incorporated into the concept. In fact, the Federal Reserve Board has published opinions interpreting the definition of "commercial loans" specifically to exclude certain activities such as issuance of certificates of deposit (Boston

Safe, 1972); broker call loans (Bradford Computer Systems, Inc., 1976); and purchase of United States government and agency obligations, certificates of deposit and time deposits, and repurchase agreements of financial institutions (Chrysler Corporation/Automotive Financial Services, Inc., 1981). We do not ignore that the Federal Reserve Board sought to limit those interpretations to their particular sets of facts; nevertheless, the Board's consistent use of a more limited definition of commercial loan led to the warranted assumption that the term included certain activities and excluded others. Now, in its analysis of the Dreyfus acquisition, the Federal Reserve Board has dramatically re-cast the definition of commercial loan by including within it certain activities that clearly had been excluded from the definition in the past. While we acknowledge the Board's authority to interpret the Bank Holding Company Act, we believe such a radical departure from the traditional view of what constitutes a commercial loan raises issues beyond the scope of regulatory interpretation.

The FDIC is in general agreement with the Federal Reserve Board about the desirability of maintaining the traditional lines of distinction between banking and commerce; however, Dreyfus is a financial services company and not a corporation engaged in general commerce. Moreover, we believe it would be inappropriate for the FDIC or the Federal Reserve Board to undertake to resolve these kinds of public policy issues. We firmly believe that Congress is the appropriate authority to reassess the statutory distinctions among banking institutions, thrifts, securities firms, other providers of financial services and commercial firms in general, and to resolve the underlying question of the activities in which banks and bank holding companies shall be permitted to engage.

The FDIC would join the Federal Reserve Board in requesting the Congress to undertake a comprehensive review of this issue. However, we could not support stop-gap or stand-alone legislation to merely redefine the term "bank" or "commercial loan." The far-reaching developments in the marketplace that have occurred over the past decade do not lend themselves to a simple solution along these lines. We

cannot ignore, for example, such mixing of federally-insured savings and loan associations with commercial enterprises as Sears and National Steel, particularly in view of the new commercial lending authority for thrifts contained in the Garn-St Germain Act. Nor can we ignore the securities firms, such as Shearson and Fidelity, that own commercial banks, as well as operate money market funds and engage in a full range of financial services. Numerous other examples exist of marketplace developments that have "outgrown" existing law. The point is, they call not for regulatory reinterpretation, but for legislative action.

In sum, while our Board was attentive to the concerns expressed in your letter of December 10, 1982, it concluded that the FDIC was constrained to follow the clear legal precedents established over the years and that any change in policy should be brought about by Congressional, not agency, action. We intend to support next year a broad-based Congressional review of the activities in which banks, thrifts, and their holding companies or affiliates should be permitted to engage.

Sincerely,

/S/ Margaret L. Egginton
MARGARET L. EGGINTON
Deputy to the Chairman

cc: Joseph Diamond

Mr. Lee J. Aubrey
Vice President
Federal Reserve Bank of Boston
Boston, Massachusetts 02106

May 18, 1972

Dear Mr. Aubrey:

The Board has considered certain questions under the Bank Holding Company Act involving Boston Safe Deposit and Trust Company. Please advise that company of the following:

It is the Board's understanding that Boston Safe Deposit and Trust Company ("Boston Safe"), a wholly-owned subsidiary of The Boston Company, Inc., is principally engaged in a trust business. Boston Safe also accepts demand deposits and makes a limited number of loans to individuals; the loans are secured by nonbusiness assets, are made as a courtesy to trust customers, and are made only on an occasional and irregular basis. However, proceeds of some such loans have been used for business purposes by the borrowers. The total amount of such loans that are for business purposes is understood to be approximately 1½ per cent of the total assets of Boston Safe. Furthermore, it is understood that Boston Safe does not solicit any loan business.

The question raised by these facts are whether loans made to individuals for business purposes and fully secured by nonbusiness assets are encompassed within the meaning of the term "commercial loans" for purposes of section 2(c) of the Bank Holding Company Act ("Act") and, if so, whether Boston Safe "engages in the business of making" such loans as the phrase is used in section 2(c) of the Act.

Section 2(c) defines "bank" as an organization which accepts demand deposits and engages in the business of making commercial loans. The Board has defined the term "commercial loans" for purposes of section 2(c) as including all loans to an individual, secured or unsecured, other than a loan the proceeds of which are used to acquire property or services used by the borrower for his own personal, family, or household purposes, or for charitable purposes. Loans to individuals for business purposes secured by nonbusiness assets fall within that definition. The Board has reconsidered

its definition to determine whether such loans should be included. Based upon the purposes of the Act and the mandate from Congress to construe all exemptions narrowly, including the exception derived from the section 2(c) definition of "bank", the Board has concluded that such loans fell within the phrase "commercial loans".

The Board has also considered whether Boston Safe "engages in the business of making" such loans and has concluded that Boston Safe does not so engage since such loans are made only occasionally, and Boston Safe makes such loans only as an accommodation to its trust customers and neither solicits such loan business nor operates a credit department.

The Board understands that Boston Safe purchases "money market instruments", such as certificates of deposit, commercial paper, and bank acceptances. In the circumstances of this case, such transactions are not regarded as commercial loans for the purposes of the Act.

On the basis of the facts presented, the Board has concluded that Boston Safe will not be regarded as engaged "in the business of making commercial loans" for purposes of the Holding Company Act by virtue of its loans to individuals, so long as Boston Safe does not make any commercial loans other than on the basis indicated above, its loan transactions are also on a limited and occasional basis for the accommodation of trust customers only, and in any event, are not in an amount in excess of 2 per cent of assets.

A further aspect of Boston Safe's operations is its engagement in Federal funds transactions which, according to Boston Safe's 1971 Report of Condition, amounted to $8 million of Federal funds sold outstanding as of December 31, 1971. The Board has previously taken the position, and continues to adhere to the position, that the sale of Federal funds constitutes an unsecured loan. The Board has concluded however that the sale of Federal funds by Boston Safe is not tantamount to the making of a commercial loan, for purposes of the Act.

Of course, Boston Safe should be advised that all the Board's conclusions in these matters are subject to revoca-

tion or amendment if any of the facts upon which those conclusions are based change in any material respect.

Very truly yours,

(signed) Michael A. Greenspan
MICHAEL A. GREENSPAN
Assistant Secretary

Date: February 10, 1981

Office Correspondence

Subject: Purchase of the Guaranteed Portions of Small Business Administration and Farmers Home Administration Loans.

ISSUE PRESENTED: Whether the proposed purchase by ______ of the United States guaranteed portions of Small Business Administration ("SBA") and Farmers Home Administration ("FmHA") loans would constitute engaging "in the business of making commercial loans" within the meaning of section 2(c) of the Bank Holding Company Act of 1956, as amended ("Act"), bringing ______ within the definition of "bank" contained in section 2(c) of the Act.

CONCLUSION: ______ proposed purchase of the guaranteed portions of SBA's and FmHA's would not constitute engaging "in the business of making commercial loans" within the meaning of section 2(c) of the Act.

BACKGROUND: By letter dated November 13, 1980 (Attachment A), the Board's Legal Division responded to the Federal Reserve Bank ______ request for an opinion on whether the proposed purchase by ______ (a trust company) of the guaranteed portions of SBA's and FmHA's would constitute engaging "in the business of making commercial loans" within the meaning of section 2(c) of the Act. According to the information received by the Board, ______ proposes to purchase guaranteed portions of SBA's and FmHA's only from nonbank dealers on the secondary market. Pursuant to federal regulations governing these lending programs, there is a strict separation of borrower, lender, and purchaser. Purchasers may not hold any interest in the underlying borrower, note, or in the collateral for the loan, other than the interest represented by the SBA or FmHA itself. In the event of a borrower's default on a loan, purchasers must look solely to the federal government for recovery. SBA's and FmHA's are general obligations of the United States secured by its full faith and credit. ______, will not originate such loans, nor will it purchase or acquire the unguaranteed portions of such loans.

DISCUSSION: The definition of "bank" contained in section 2(c) of the Act was amended in 1970. The original definition,

adopted by Congress in 1966, "... was designed to include commercial banks and to exclude those institutions not engaged in commercial banking, since the purpose of the act was to restrain undue concentration of commercial banking resources and to prevent possible abuses related to the control of commercial credit." However, the Board "... noted that this definition may be too broad and may include institutions which are not in fact engaged in the business of commercial banks in that they do not make commercial loans."[1] Therefore, Congress added a second test, "engages in the business of making commercial loans," to its original definition of bank as "any institution ... which accepts deposits that the depositor has a legal right to withdraw on demand." Congress cautioned that any exemption from its definition should be made "as narrowly as possible in order that all bank holding companies which should be covered under the Act in order to protect the public interest will, in fact, be covered."[2]

In determining what constitutes "commercial lending", the Board has looked to the purposes for which a loan was made, finding that lending for personal, family or household purposes is not commercial lending. (*Greater Providence Deposit Corp.*, letter dated July 1, 1971; *Boston Safe Deposit and Trust Company*, letter dated June 8, 1972). The Board also has concluded that, although commercial in nature, the purchase of federal funds, money market instruments (certificates of deposit, commercial paper, and bankers acceptances) are not considered commercial loans *for the purposes of section 2(c) of the Act*, despite the fact that for other statutory and regulatory purposes these instruments may be considered commercial loans. (*Boston Safe*) Likewise, Board staff determined that broker call loans and sold securities transactions are not considered commercial loans *for the purposes of section 2(c) of the Act.* (*Bradford Trust Company*, letter dated January 26, 1976.) These determinations were based upon the specific characteristics of these instruments and transactions involving them. In each instance, the Board

---

[1] S. Rep. No. 91-1084, 91st Cong., 2nd Sess. (1970), p. 24.

[2] H.R. Rep. No. 91-1747, 91st Cong., 2nd Sess. (1970), p. 23.

or its staff found that these transactions did not involve the particular type of lender-borrower relationship that is one of the characteristics of commercial loans, and which presents the possibility of abuses relating to control of commercial credit that concerned Congress when it adopted the commercial lending test. These decisions subsequently were incorporated into the description of permissible activities for a section 4(c)(8) trust company contained in section 225.4(a)(4)(iii) of the Board's Regulation Y, 12 C.F.R. § 225.4(a)(4)(iii).

Finally, the Board found that loans made by a trust company to individuals for commercial purposes on an occasional basis as a courtesy to its trust customers would not be regarded as "engaging in the business of making commercial loans" for purposes of section 2(c) of the Act as long as the trust company *"does not make any commercial loans other than on the basis indicated above, its commercial bank transactions are on a limited and occasional basis for the accommodation of trust customers only, and in any event, are not in an amount in excess of 2 percent of assets." (Boston Safe.)*[3]

January 26, 1976

Michael A. Greenspan, Esq.
Metzger, Noble, Schwartz & Kemplar
One Farragut Square South
Washington, D.C. 20006

Dear Mr. Greenspan:

This is in response to your request for the Legal Division's opinion on the status of your client Bradford Computer Systems, Inc. ("Bradford") under the Bank Holding Company Act of 1956, as amended ("Act") in light of certain proposed activities of Bradford and/or its subsidiary Bradford Trust Company ("Company").

Under section 3(a)(1) of the Act (12 U.S.C. 1842(a)(1)) it is unlawful, except with prior Board approval, for any action to be taken that causes any company to become a bank holding company. Since a bank holding company is defined to mean any company that has "control" over a "bank", as those terms are defined in the Act, Bradford would have to file an application to become a bank holding company if Company proposed to engage in activities that would make it a "bank" within the meaning of section 2(c) of the Act or if Bradford proposed to acquire control of another institution that would be defined as a "bank" under the Act. The term "bank" is defined in section 2(c) of the Act (12 U.S.C. 1841(c)) to mean "... any institution organized under the laws of the United States, any State of the United States ... which (1) accepts deposits that the depositor has a legal right to withdraw on demand, and (2) engages in the business of making commercial loans...."

It is stated in your correspondence that you have advised Bradford that if Company conducts only those activities permissible for a nonbanking trust company subsidiary of a bank holding company under section 4(c)(8) of the Act and § 225.4(a)(4) of Regulation Y, then Bradford does not have to apply to become a bank holding company. You base this opinion on the fact that under section 4(c)(8) of the Act and Regulation Y, bank holding companies can acquire voting share interests in trust companies located outside of their State of principal banking operations. Since section 3(d) of

the Act prohibits the Board from approving any bank holding company acquisition of any voting shares of, interest in, or all or substantially all of the assets of an additional "bank" located outside of a bank holding company's State of principal banking operations, as determined in that section, it is your opinion that if a trust company limits its activities to those prescribed under section 4(c)(8) of the Act and section 2245.4(a)(4) of Regulation Y, the Board has determined that it is thus not a "bank" within the meaning of the Act. You request that the Legal Division concur in this opinion and concur also with your opinion that Company may make "broker call loans" because such loans are not commercial loans, based in part upon your opinion that nonbanking trust company subsidiaries of bank holding companies may make such loans under section 225.4(a)(4) of Regulation Y. You also request the Legal Division's concurrence with your opinion that if Company engages in certain so-called "sold securities transactions", as hereinafter described, these specific activities would not cause Company to be engaged in the business of making commercial loans within the meaning of section 2(c). In this regard, you base your opinion on your view that these sold security transactions either should be regarded as broker call loans or should not in any event be regarded as a form of commercial loan within the meaning of section 2(c) of the Act.

The Legal Division generally concurs with your opinion that if a trust company confines its activities to those specified under section 225.4(a)(4) of the Regulation Y, then it does not come within the definition of "bank" in section 2(c) of the Act. With respect to the permissible "broker call loan" activities of a trust company under the regulation, section 225.4(a)(4)(iii) of Regulation Y provides that a trust company in which a bank holding company has an interest may engage in the "making of call loans to securities dealers or purchase of money market instruments such as certificates of deposit, commercial paper, government or municipal securities, and bankers' acceptances". In the Legal Division's judgment, the making of brokers' call loans by trust company subsidiaries of bank holding companies is permissible under the foregoing regulation, based on its understand-

ing that such call loans constitute merely a method of investing a trust company's idle funds and do not constitute a type of revolving credit business loan.[1] Essentially, in the Legal Division's opinion, nonbank trust companies owned by bank holding companies are permitted to make call loans to securities dealers under section 225.4(a)(4)(iii) of Regulation Y because this type of loan is distinguishable from the ordinary commercial loan in that such call loans are entered into on a daily renewable basis with both parties having the option not to renew, are made primarily as a means of temporarily investing idle funds, and are viewed by the lending institution as an alternative to the purchase of money market instruments, such as commercial paper or bankers' acceptances. This type of "call loan" is thus viewed as a passive medium of investment, with the lender making a daily investment judgment based on its analysis of money market rates. "Call loans" thus do not appear to have the close lender-borrower relationship that is one of the characteristics of commercial loans and which presents the possibility of abuses relating to the control of commercial credit that concerned the Congress in adopting the commercial lending test.[2] Thus to the extent that Company engages in brokers' call loans of this character, the Legal Division believes that such activities would not cause it to be engaged in the business of making commercial loans.

With respect to "sold security transactions", it is understood from your description that these transactions would be conducted as follows: A selling broker, for a fee, delivers securities he has sold to Company, with instructions attached that contain the name and address of the out-of-town buyer, the amount to be paid, and the name of the bank or other institution that will take payment. Also attached to the securities is a negotiable draft for collection, which incorporates the foregoing information and which is entered as a receivable on the trust company's books. The securities are for-

[1] See the Board's Order of December 23, 1975 approving The Toronto-Dominion Bank's retention of the Toronto Dominion Bank Trust Company, New York, New York under § 4(c)(8) of the Act and § 225.4(a)(4) of Regulation Y.

[2] See S. Rep. No. 91-1084, 91st Cong., 2d Sess., p. 248.

warded to the named bank for delivery and the draft is presented to said bank for collection. The entire process normally takes two days. As is customery for other trust companies, it is proposed that Company, at the broker's request, give the broker immediate credit on the draft.

In the Legal Division's opinion, this type of transaction does not appear to involve a broker call loan within the meaning of section 225.4(a)(4)(iii) of Regulation Y, as it is not a means for temporarily investing idle funds of the trust company. Rather, this transaction essentially involves giving a broker immediate credit in his account for a draft drawn on another trust company or bank, such draft being drawn in payment for securities sold by the broker. You state that it is your view that, as in the case of immediate credit given on a check, the Company will look primarily for repayment to the bank on which the draft is drawn, and not to the broker. Based on the foregoing, the Legal Division believes that should Company engage in "sold security transactions" with its broker customers, as described herein, this activity, in and of itself, would not appear to cause Company to be engaged in the business of making commercial loans within the meaning of section 2(c).

Apart from your requests pertaining to "broker call loans", I note also that you have indicated that Bradford proposes to organize a so-called limited purpose national bank under a charter issued by the Comptroller of the Currency to engage in trust company activities. In this regard, you have requested staff concurrence of your view that the charter powers of a company do not determine whether it is a "bank" within the meaning of section 2(c) of the Act, but rather it is the specific activities of the company that is determining. You base your opinion on a Board letter of June 7, 1972 to Mr. Lawrence Stone, General Counsel of the Federal Reserve Bank of Boston, regarding the status of Boston Safe Deposit and Trust Company under section 2(c) of the Act. You state that you are interested in obtaining the staff's views because the Office of the Comptroller of the Currency believes that such an institution owned by Bradford would be in the public interest but is uncertain whether the charter or by-laws should be restricted in order

to keep the institution from being a "bank" under the Act or whether the institution should simply not exercise the full powers given. From an administrative and regulatory standpoint, the Legal Division believes that the former course of action i.e., actually limiting the charter powers of the organization, would be the preferable course of action and would best fulfill the purposes of the Act and the Board's regulations. The Legal Division chooses at this time not to express any views on your opinion that the charter powers of a company do not determine whether it is a "bank", as it feels there are policy aspects to such a general position that should be considered by the Board.

Pursuant to your requests, the views expressed herein are, of course, solely those of the Board's Legal Division and, as such, do not constitute an interpretation by the Board of the provisions of the Act or Regulation Y or a Board decision or ruling on the facts presented.

Very truly yours,

(signed) Baldwin B. Tuttle
BALDWIN B. TUTTLE
Deputy General Counsel

ADDENDUM H

November 13, 1980

Mr. William N. McDonough
Assistant General Counsel
Federal Reserve Bank of Boston
Boston, Massachusetts 02106

Dear Bill:

This is in response to your letters of June 26, and July 7, 1980, in which you request the opinion of the Board's Legal Division as the whether the proposed purchase by ______ ("Company") of the guaranteed portions of Small Business Administration and Farmers Home Administration loans would constitute engaging "in the business of making commercial loans" within the meaning of section 2(c) of the Bank Holding Company Act of 1956, as amended ("Act"), bringing Company within the definition of "bank" contained in section 2(c) of the Act.

According to the information you have forwarded to the Board, Company proposes to purchase those portions of loans made by the Small Business Administration and the Farmers Home Administration that are fully guaranteed by the United States, pursuant to programs administered by the two agencies. These guaranteed portions, commonly known as "SBA's" and "FmHA's", are sold by nonbank dealers on the secondary market. Pursuant to federal regulations governing these lending progress, there is a strict separation of borrower, lender, and purchaser. Purchasers may not hold any interest in the underlying borrower, note, or in the collateral for the loan, other than the interest represented by the SBA or FmHA itself. In the event of a borrower's default on a loan, purchasers must look solely to the federal government for recovery. Company has represented that all of its purchases of SBA's and FmHA's will be made from nonbank dealers in the secondary market. Company will not originate such loans, nor will it purchase or acquire the unguaranteed portions of such loans.

The Legal Division concurs in your view that Company's purchase of SBA's and FmHA's, in the manner outlined above, would not constitute engaging "in the business of making commercial loans" within the meaning of section 2(c) of the Act. Rather, the purchase of SBA's and FmHA's by Company as described appears to be a passive medium of investment, representing an alternative to the investment of Company's idle funds in government securities, inasmuch as SBA's and FmHA's are similar to government securities in that they are general obligations of the United States secured by its full faith and credit. Moreover, SBA's and FmHA's do not appear to involve the particular type of lender-borrower relationship that is one of the characteristics of commercial loans, and which presents the possibility of abuses relating to the control of commercial credit that concerned Congress when it adopted the commercial lending test, found in the Act. (See S. Rep. No. 91-1084, 91st Cong., 2nd Sess., p. 248.)

Therfore, the Legal Division concludes that the proposed purchase by Company of SBA's and FmHA's would not bring Company within the definition of "bank" contained in section 2(c) of the Act. If you have any further questions concerning this matter, please contact Ms. Bronwen Mason (202/452-3564) or Ms. Sara Kelsey (202/452-3236) of the Board's Legal Division.

Very truly yours,

(signed) Robert E. Mannion
ROBERT E. MANNION
Deputy General Counsel

EDITOR'S NOTE

THE FOLLOWING PAGES WERE POOR HARD COPY AT THE TIME OF FILMING. IF AND WHEN A BETTER COPY CAN BE OBTAINED, A NEW FICHE WILL BE ISSUED.

ADDENDUM I

ENTER SELECTION # OR DONE--> 1

VALLEY NATIONAL BANK		BANK ADMINISTRATION INSTITUTE	CA1285
SALINAS CA		INDIVDUAL BANK PROFILE -- 1982	RES. CLASS 5
AVERAGE ASSETS		INCOME/EXPENSE	
1 CASH & DUE FROM BANKS	19,473	32 INTEREST & FEES ON LOANS	7,277
2 INTEREST-BEARING BALANCES	0	33 INT ON BALANCES WITH BKS	1,137
		34 INT ON FED FUNDS SOLD	911
3 U.S.TREASURY SECURITIES	149	35 INT ON U.S. SECURITIES	265
4 SEC - OTHER U S AGENCIES	2,795	37 INT ON OBLIG OF STATES	896
5 OBLIGATIONS OF STATES	13,159	38 INT ON OTHER SECURITIES	22
6 OTHER SECURITIES	0	39 INC FRM DIRECT LEASE FIN	366
TOTAL INVSTMT SECURITIES	16,103	TOTAL INTEREST INCOME	10,874
7 FED FUNDS SOLD	5,304		
		40 INT ON TIME DEP OVR 100M	490
8 REAL ESTATE LOANS--RES ID	7,578	41 INT ON OTHER TIME & SVGS	5,110
9 REAL ESTATE LOANS--OTHER	9,551	42 INT ON FOREIGN DEPOSITS	0
10 INSTALLMENT LOANS	28,908	43 INT ON FED FUNDS PURCHAS	0
11 COMMERCIAL AND INDUSTRIAL	0	44 INT ON OTHR BORRWD MONEY	82
12 AGRICULTURAL LOANS	0	45 INT ON CAPITAL NOTES	0
13 OTHER LOANS	11,456	TOTAL INTEREST EXPENSE	5,682

ENTER MORE OR DONE--> MORE

TOTAL LOANS GROSS	57,493		
14 LESS: UNEARNED DISCOUNT	5,875	NET INTEREST MARGIN	5,192
TOTAL LOANS	51,618		
15 LESS: ALLOW/LOAN LOSS	373	46 TRUST DEPARTMENT INCOME	0
TOTAL LOANS NET	51,243	47 OTHER OPERATING INCOME	1,613
16 DIRECT LEASE FIN	2,250	TOT OTHR OPER INC	1,613
17 PROPERTY	2,910		
18 OTHER ASSETS	2,857	48 SALARIES AND BENEFITS	3,541
		49 BANK PREMIS & FURNITURE	1,309
TOTAL AVERAGE ASSETS	100,140	50 LOAN LOSS PROVISION	560
		51 OTHER EXPENSE	3,705
AVERAGE LIABILITIES		OTHER OPERATING EXPENSE	9,215
19 DEMAND DEPOSITS -- IPC	27,014	INC BEF TAX & SEC TRANS	-2,411
20 PUBLIC FUNDS--DEMAND	132		
21 OTHER DEMAND DEPOSITS	1,220	52 APPLICABLE INCOME TAXES	0
TOTAL DEMAND DEPOSITS	28,367	53 INCOME BEFORE SEC GAINS	-2,411
22 TIME & SAVINGS--IPC	63,687	54 SEC GAINS AND LOSSES	-2
23 PUBLIC FUNDS--TIME	0	55 EXTRAORDINARY ITEMS	0
24 TIME DEPOSITS OVER 100M	3,635		
25 OTHER TIME & SAVINGS	0	NET INCOME	-2,413

ENTER MORE OR DONE--> MORE

TOTAL DOM TIME & SAV	63,686		
TOTAL DOM DEPOSITS	92,053	MISCELLANEOUS	
26 FOREIGN DEPOSITS	0		
TOTAL DEPOSITS	92,053	56 CASH DIV--COMMON STOCK	
		57 REC CREDT-BAD DEBT ALLOW	15
27 FED FUNDS PURCHASED	0	58 LOSSES CHRGD TO BAD DEBT	65
28 MORTGAGE INDEBTEDNESS	531	59 INC BEF SEC GAIN--1981	0
29 OTHER LIABILITIES	1,251	60 NET INCOME--1981	56
TOTAL LIABILITIES	93,835	61 AVERAGE ASSETS--1981	97,22
30 CAPITAL NOTES & DEBENTS	0		
31 EQUITY CAPITAL--TOTAL	6,304		
TOT AVG LIAB, CAP, RES	100,140		

1014 DD

```
PERFORMANCE (% OF ASSETS)                    USE OF FUNDS
                                             (% EARNING ASSETS)
 1 INTEREST INCOME (FTE)          11.61%
 2 INTEREST EXPENSE                5.67% 35 INVESTMENT SECURITIES        21.39%

ENTER MORE OR DONE--> MORE

 3 NET INTEREST MARGIN             5.94% 36 FED FUNDS SOLD                7.04%
 4 TRUST INCOME                    0.00% 37 TOTAL LOANS                  73.16%
 5 SERVICE CHRG ON DEP*            1.13% 38 RESERVE FOR LOAN LOSS         0.45%
 6 OTHER NON-INT INCOME            0.47% 39 REAL ESTATE LOANS-RESID       3.33%
 7 SALARIES AND BENEFITS           3.53% 40 REAL ESTATE LOANS-OTHER      11.76%
 8 OCCUP, FURN, EQUIP EXP          1.30% 41 COMM & INDUSTRIAL LOANS       0.00%
 9 LOAN LOSS PROVISION             0.65% 42 PERSONAL LOANS               35.62%
10 OTHER NON-INT EXPENSE           3.69% 43 AGR/LEASE FIN/OTHER LOAN     16.89%
11 LESS FTE ADJUSTMENT             0.76%
12 TAX PROVISION                   0.00%  SOURCE OF FUNDS
13 RETURN ON ASSETS--OP INC       -2.40%  (% EARNING ASSETS)
14 RETURN ON ASSETS--NET INC      -2.40%
15 RETURN ON EQUITY--NET INC     -38.27% 44 DEMAND DEPOSITS IPC*         37.50%
                                         45 PUB FUNDS DEMAND DEPS         0.17%
YIELDS AND RATES                         46 TOTAL DEMAND DEPOSITS*       37.69%
                                         47 SAVINGS DEPOSITS* IPC        43.36%
16 TAX EQU YIELD-EARN ASSETS      15.45% 48 TIME DEPOSITS IPC*           41.24%
17 BREAK EVEN YIELD               17.64% 49 PUB TIME & SAVG DEPS          0.00%
18 YIELD ON INVEST SEC (FTE)      11.93% 50 TOTAL TIME & SAVG DEPS       84.60%
19 YIELD ON LOANS                 14.09% 51 MEMO: MONEY MARKET CDS       26.61%
20 NET CHRG-OFFS % AV LOANS        0.96% 52 MEMO: TIME DEPS OVR 100M      4.82%

ENTER MORE OR DONE--> MORE

21 LOAN LOSS PROV % AV LOANS       1.27% 53 FOREIGN DEPOSITS              0.00%
22 RATE ON TIME & SAVINGS          8.79% 54 TOTAL DEPS (FGN & DOM)      122.29%
23 RATE ON TOTAL INT FUNDS         8.84% 55 BORROWINGS                    0.70%
24 INT EXPENSE % EARN ASSETS       7.54% 56 NET LARGE LIABILITIES         0.00%
                                         57 NON-RATE ASSET/LIAB GAP      14.69%
CAPITAL POSITION
                                          GROWTH STATISTICS
25 EFFECTIVE TAX RATE-OP INC       0.00%
26 CASH DIV % OPER INC             0.00% 58 INCOME BEF SEC TRAN 1-YR       N/A
27 CAPITAL FORMATION RATIO       -38.27% 59 NET INCOME 1-YR                N/A
28 EQUITY CAPITAL % ASSETS         6.29% 60 AVERAGE ASSETS 1-YR          10.03%
                                         61 INCME BEF SEC TRANS 5-YR       N/A
PRODUCTIVITY                             62 NET INCOME 5-YR                N/A
                                         63 AVERAGE ASSETS 5-YR          15.33%
29 EARNING ASSETS % ASSETS        75.16%
30 NON-INT CASH&DUE % ASSETS      19.44%  * DOMESTIC ONLY
31 NON-INT INC % NON-INT EXP      18.85%
32 PERSONNEL EXP/EMPLOYEE       $19,037
33 EMPLOYEES PER MILL ASSETS       1.85
34 NON-INT INC % SALARIES         45.55%

ENTER ST/FDIC NO, ST/CITY/INITIAL, OR DONE --> MI/DETROIT/A
NO MATCH FOUND
ENTER ST/FDIC NO, ST/CITY/INITIAL OR DONE --> CA/CONCORD/F
NO MATCH FOUND
ENTER ST/FDIC NO, ST/CITY/INITIAL OR DONE --> CA/CARLSBAD/W
NO MATCH FOUND
```

1014 EE

ENTER SELECTION # OR DONE--> 1

ASSOCIATES NATIONAL BANK   CA
CONCORD
BANK ADMINISTRATION INSTITUTE   CA0223
INDIVDUAL BANK PROFILE -- 1982   RES. CLASS 3

AVERAGE ASSETS		INCOME/EXPENSE	
1 CASH & DUE FROM BANKS	3,201	32 INTEREST & FEES ON LOANS	4,000
2 INTERST-BEARING BALANCES	0	33 INT ON BALANCES WITH BKS	703
		34 INT ON FED FUNDS SOLD	563
3 U.S.TREASURY SECURITIES	12	35 INT ON U.S. SECURITIES	38
4 SEC - OTHER U S AGENCIES	264	37 INT ON OBLIG OF STATES	0
5 OBLIGATIONS OF STATES	0	38 INT ON OTHER SECURITIES	24
6 OTHER SECURITIES	0	39 INC FRM DIRECT LEASE FIN	137
TOTAL INVSTMT SECURITIES	276	TOTAL INTEREST INCOME	5,465
7 FED FUNDS SOLD	3,090		
		40 INT ON TIME DEP OVR 100M	1,217
8 REAL ESTATE LOANS--RESID	70	41 INT ON OTHER TIME & SVGS	493
9 REAL ESTATE LOANS--OTHER	0	42 INT ON FOREIGN DEPOSITS	0
10 INSTALLMENT LOANS	1,652	43 INT ON FED FUNDS PURCHAS	1
11 COMMERCIAL AND INDUSTRIAL	0	44 INT ON OTHR BORRWD MONEY	2
12 AGRICULTURAL LOANS	0	45 INT ON CAPITAL NOTES	0
13 OTHER LOANS	25,463	TOTAL INTEREST EXPENSE	1,713

ENTER MORE OR DONE--> MORE

TOTAL LOANS GROSS	27,215		
14 LESS: UNEARNED DISCOUNT	0	NET INTEREST MARGIN	3,752
TOTAL LOANS	27,215		
15 LESS: ALLOW/LOAN LOSS	1,122	46 TRUST DEPARTMENT INCOME	0
TOTAL LOANS NET	26,091	47 OTHER OPERATING INCOME	748
16 DIRECT LEASE FIN	780	TOT OTHR OPER INC	748
17 PROPERTY	770		
18 OTHER ASSETS	2,795	48 SALARIES AND BENEFITS	588
		49 BANK PREMIS & FURNITURE	192
TOTAL AVERAGE ASSETS	37,003	50 LOAN LOSS PROVISION	1,582
		51 OTHER EXPENSE	2,069
AVERAGE LIABILITIES		OTHER OPERATING EXPENSE	4,431
19 DEMAND DEPOSITS -- IPC	1,162	INC BEF TAX & SEC TRANS	69
20 PUBLIC FUNDS--DEMAND	18		
21 OTHER DEMAND DEPOSITS	825	52 APPLICABLE INCOME TAXES	-26
TOTAL DEMAND DEPOSITS	2,008	53 INCOME BEFORE SEC GAINS	95
22 TIME & SAVINGS--IPC	16,111	54 SEC GAINS AND LOSSES	0
23 PUBLIC FUNDS--TIME	49	55 EXTRAORDINARY ITEMS	0
24 TIME DEPOSITS OVER 100M	10,895		
25 OTHER TIME & SAVINGS	0	NET INCOME	95

ENTER MORE OR DONE--> MORE

TOTAL DOM TIME & SAV	16,159		
TOTAL DOM DEPOSITS	18,167	MISCELLANEOUS	
26 FOREIGN DEPOSITS	0		
TOTAL DEPOSITS	18,167	56 CASH DIV--COMMON STOCK	0
		57 REC CREDT-BAD DEBT ALLOW	7
27 FED FUNDS PURCHASED	0	58 LOSSES CHRGD TO BAD DEBT	187
28 MORTGAGE INDEBTEDNESS	0	59 INC BEF SEC GAIN--1981	396
29 OTHER LIABILITIES	1,998	60 NET INCOME--1981	396
TOTAL LIABILITIES	20,165	61 AVERAGE ASSETS--1981	18,645
30 CAPITAL NOTES & DEBENTS	0		
31 EQUITY CAPITAL--TOTAL	16,838		
TOT AVG LIAB, CAP, RES	37,003		

1014FF

PERFORMANCE (% OF ASSETS)

1 INTEREST INCOME (FTE)	14.76%
2 INTEREST EXPENSE	4.62%

ENTER MORE OR DONE--> MORE

3 NET INTEREST MARGIN	10.13%
4 TRUST INCOME	0.00%
5 SERVICE CHRG ON DEP♦	0.18%
6 OTHER NON-INT INCOME	1.83%
7 SALARIES AND BENEFITS	1.58%
8 OCCUP, FURN, EQUIP EXP	0.51%
9 LOAN LOSS PROVISION	4.27%
10 OTHER NON-INT EXPENSE	5.59%
11 LESS FTE ADJUSTMENT	0.00%
12 TAX PROVISION	-0.07%
13 RETURN ON ASSETS--OP INC	0.25%
14 RETURN ON ASSETS--NET INC	0.25%
15 RETURN ON EQUITY--NET INC	0.56%

YIELDS AND RATES

16 TAX EQU YIELD-EARN ASSETS	17.42%
17 BREAK EVEN YIELD	17.20%
18 YIELD ON INVEST SEC (FTE)	13.76%
19 YIELD ON LOANS	14.69%
20 NET CHRG-OFFS % AV LOANS	0.66%

ENTER MORE OR DONE--> MORE

21 LOAN LOSS PROV % AV LOANS	5.81%
22 RATE ON TIME & SAVINGS	10.59%
23 RATE ON TOTAL INT FUNDS	10.60%
24 INT EXPENSE % EARN ASSETS	5.46%

CAPITAL POSITION

25 EFFECTIVE TAX RATE-OP INC	-37.68%
26 CASH DIV % OPER INC	0.00%
27 CAPITAL FORMATION RATIO	0.56%
28 EQUITY CAPITAL % ASSETS	45.50%

PRODUCTIVITY

29 EARNING ASSETS % ASSETS	84.75%
30 NON-INT CASH&DUE % ASSETS	8.65%
31 NON-INT INC % NON-INT EXP	26.25%
32 PERSONNEL EXP/EMPLOYEE	$4,421
33 EMPLOYEES PER MILL ASSETS	3.59
34 NON-INT INC % SALARIES	127.21%

USE OF FUNDS
(% EARNING ASSETS)

35 INVESTMENT SECURITIES	0.28%
36 FED FUNDS SOLD	9.85%
37 TOTAL LOANS	85.68%
38 RESERVE FOR LOAN LOSS	3.57%
39 REAL ESTATE LOANS-RESID	0.22%
40 REAL ESTATE LOANS-OTHER	0.01%
41 COMM & INDUSTRIAL LOANS	0.00%
42 PERSONAL LOANS	5.36%
43 AGR/LEASE FIN/OTHER LOAN	83.68%

SOURCE OF FUNDS
(% EARNING ASSETS)

44 DEMAND DEPOSITS IPC♦	6.33%
45 PUB FUNDS DEMAND DEPS	0.05%
46 TOTAL DEMAND DEPOSITS♦	6.40%
47 SAVINGS DEPOSITS♦ IPC	6.20%
48 TIME DEPOSITS IPC♦	45.16%
49 PUB TIME & SAVG DEPS	0.15%
50 TOTAL TIME & SAVG DEPS	51.52%
51 MEMO: MONEY MARKET CDS	4.22%
52 MEMO: TIME DEPS OVR 100M	34.74%
53 FOREIGN DEPOSITS	0.00%
54 TOTAL DEPS (FGN & DOM)	57.92%
55 BORROWINGS	0.04%
56 NET LARGE LIABILITIES	24.92%
57 NON-RATE ASSET/LIAB GAP	48.43%

GROWTH STATISTICS

58 INCOME BEF SEC TRAN 1-YR	-76.01%
59 NET INCOME 1-YR	-76.01%
60 AVERAGE ASSETS 1-YR	107.64%
61 INCME BEF SEC TRANS 5-YR	161.68%
62 NET INCOME 5-YR	161.69%
63 AVERAGE ASSETS 5-YR	321.06%

♦ DOMESTIC ONLY

1014EG

ADDENDUM J

March 12, 1981

Mr. Robert C. Zimmer
Zimmer & Einhorn
Suite 370
2501 M Street, N.W.
Washington, D.C., 20037

Dear Mr. Zimmer:

This is to advise you that the Board has reviewed the status of your client, Associates First Capital Corporation ("Associates"), a subsidiary of Gulf & Western, under the Bank Holding Company Act of 1956, as amended ("Act"), following its acquisition of Fidelity National Bank, Concord, California ("FNB"). The Board's review is based upon your submissions to the Board, including a letter to Mr. Robert E. Mannion dated February 5, 1981, a copy of FNB's management policy statement dated September 1, 1980, and commitments made to the Comptroller of the Currency dated August 4 and 12, 1980.

The Board understands that FNB, a national bank, divested itself of all of its commercial loans prior to its acquisition by Associates. Associates commits that FNB will make no commercial loans, and in its management policy statement for FNB indicates that FNB will strictly limit its lending to loans for personal, family, household or chariable purposes. FNB intends to document its compliance with these commitments by requiring a statement from each loan applicant acknowledging the purpose of the loan and, if there is any question regarding a borrower's purpose, the loan will not be made without the prior approval of FNB's board of directors.

In order to separate completely its deposit-taking activities from any commercial lending activities of Associates and any of its affiliates, FNB will in no way supply or maintain the availability of funds to Associates or its affiliates except in the form of dividends payable to Associates (as well as certain transactions between FNB and affiliates pertaining primarily to payroll and employee benefits completed monthly on a fee basis). Associates will not permit any of its nonbanking affiliates to enter into any extensions of credit or in lending or deposit relationships, joint ventures, or activities performed on a fee basis involving FNB, unless permitted by applicable statutes, rules, or regulations.

In addition, no commercial loan inquiries, opportunities or referrals will be directed by FNB to any affiliates of Associates and no deposits of FNB will be loaned to or used for the benefit of any activity of Associates, or its commercial operating subsidiary, Associates Commercial Corporation, or any other Associates activity which could be construed to involve commercial loans. FNB has charged its officers and management with the responsibility for implementing its management policies and has adopted a number of procedures to internally monitor compliance.

Under section 3(a)(1) of the Act (12 U.S.C. §1842(a) (1)), it is unlawful, except with prior Board approval, for any action to be taken that causes any company to become a bank holding company. Since a bank holding company is defined under the Act as any company that controls a "bank", Associates would have had to obtain the Board's prior approval to become a bank holding company before acquiring FNB, if FNB were a "bank" under the Act. The term "bank" is defined in section 2(c) of the Act (12 U.S.C. §1841(c)) to mean ". . any institution. . . which (1) accepts deposits that the depositor has a legal right to withdraw on demand, and (2) engages in the business of making commercial loans."

Based upon the information contained in your submissions, it appears that FNB is not a "bank" within the meaning of section 2(c) of the Act, since it has divested itself of its commercial loan portfolio, has committed that it will not engage in commercial lending, and intends to limit its lending to loans to individuals for personal, family, household or charitable purposes. Moreover, it appears that FNB has made adequate provision to insure that its demand deposit-taking functions will remain separate from the commercial lending functions of its affiliates, based upon FNB's commitments that it will not supply or maintain the availability of funds (except through dividends) to any affiliate that makes commercial loans.

Based upon the above representations, the Board has concluded that FNB is not a "bank" within the meaning of section 2(c) of the Act, and therefore Associates was not required by the Act to obtain the Board's approval prior to its acquisition of FNB. This determination is based expressly upon the facts summarized herein and the commitments and representations contained in the correspondence referenced above and any material change therefrom could result in a different conclusion.

Very truly yours,
JAMES MCAFEE
Assistant Secretary of the Board

ADDENDUM K
American Banker, July 13, 1981

HOUSEHOLD FINANCE PARENT TO ENTER BANKING BY ACQUISITION

By James Rubenstein

CHICAGO—Household International Inc., a Chicago-based conglomerate and parent of Household Finance Corp., the nation's third largest consumer finance firm, announced plans last week to enter retail banking through the acquisition of a small California bank.

In the second bank-purchase agreement of its kind involving a consumer finance firm, Household said it seeks to acquire the $88.1 million deposit Valley National Bank, of Salinas.

Household said its planned acquisition of the bank, in a $20.3 million tender offer to shareholders, has already been approved by the Comptroller of the Currency.

Complying with a Federal Reserve Board ruling last March on such acquisitions by nonbank firms, Household said if the purchase is consummated it will divest Valley National's commercial portfolio and retain the institution as a "consumer bank."

In the March ruling,—also dealing with another small California bank, the $10 million-deposit Fidelity National Bank, of Concord—the Fed upheld its purchase by Associates First Capital Corp., the Dallas consumer finance subsidiary of Gulf & Western Corp.

The Comptroller had approved that acquisition in August 1980 provided Fidelity spin off its commercial banking operations, which it has since done.

Has 7 Branches

Valley National, founded in 1964, and located in central California, has assets of $98 million and operates seven branches in the Salinas-Monterey-Watsonville area.

In a formal statement put out by Household International, the diversified Prospect Heights, Ill., firm said Valley National "conducts normal banking operations but focuses on retail lending an deposits."

Household International is a Fortune 500 firm with $7 billion in assets controlling a diverse assortment of businesses ranging from plumbing fixtures to insurance.

It owns City Products Co., a large merchandiser, National Car Rental, Ben Franklin Stores, and last month required Wallace-Murray Corp.

Household Finance—with over 2,000 consumer loan offices—has capital funds of $1.58 billion.

Cash Tender Offer

On the Valley National purchase, Household International said it is extending a $65.50 cash tender offer for all of the 310,000 outstanding shares of the Salinas bank.

The announcement said directors of the bank have entered into an agreement with Household to sell 18% of shares owned by them and also have recommended the offer to shareholders.

"While today Household Finance operates some 35 units in the areas of merchandising, manufacturing, and transportation, we have remained dedicated to maintaining our leadership position in financial services through expansion and selected acquisitions," stated G.R. Ellis, chairman of the board and chief executive officer of Household International.

"Banking will not be new to us. We began HFC Trust Ltd. in the United Kingdom in 1973, and today we serve the U.K. through 107 offices of this consumer banking operation," said Household.

"This acquisition is designed to further HFC's goals of providing a full range of financial services to our customers," stated W.D. Hendry, president of Household Finance.

Household's "success" in this area "has led us to believe banking is an essential element of our plans to provide a totally comprehensive program of financial services," Mr. Hendry said.

Edward L. Evans, president of Valley National, said discussions with Household began eight months ago after his bank was chosen by the Chicago firm as the most suitable candidate for takeover.

"I think there were seven or eight other banks that showed up on somebody's screen, and through the process of elimination we were chosen," said Mr. Evans.

Aiding Household in the selection process was Morgan Guaranty Trust Co. of New York, through its investment advisory services which retain Household as a client, Mr. Evans said.

5-State Survey

As part of the "finding" process, Morgan Guaranty had conducted a survey of five states, Mr. Evans said.

Household, he said, apparently seeks to own a national bank "and pay this kind of price" to take advantage "of the deposit taking function."

Household already has a significant California base with 265 offices in the state with $600 million in loans, Mr. Evans said.

"Our bank is strategically located in the central part of the state and that may have been another factor in their thinking," he said.

In acquiring the Salinas bank, Mr. Evans surmised Household might seek to expand Valley National's seven branches into a statewide system.

Household may also have chosen to enter retail banking in this manner "to use our charge card operation."

Valley National offers both MasterCard and Visa with 8,000 accounts and a $2.5 million portfolio.

Under the agreement with Valley NB and in compliance with the Fed, Household will dispose of the bank's commercial assets which amount to 10% of the portfolio.

Valley NB can retain consumer leasing, direct consumer loans and real estate loans, said Mr. Evans.

The Salinas banker said another California bank would likely be a buyer of the commercial loans "but those arrangements are not known to us."

Mr. Evans, who has been president of the bank since its founding, said all of the bank's management intends to stay following the consumation of the transaction next month.

Application to acquire the bank was made with the Comptroller March 23 under the Change of Control Act with the 60-day waiting period expiring May 23, said a Household spokesman.

The Household tender offer expires Aug. 5. ■

ADDENDUM L

American Banker, September 30, 1982

FED ALLOWS CITICORP TO ACQUIRE FIDELITY

The Federal Reserve Board on Tuesday issued an order allowing Citicorp, New York, to acquire Fidelity Savings & Loan Association, San Francisco, adding several conditions designed to preserve Fidelity's character as a thrift. An appendix to the order will appear in the issue of Monday, Oct. 4.

Citicorp, New York, New York, a bank holding company within the meaning of the Bank Holding Company Act (the "BHC Act"), has applied for the Board's approval under section 4(c)(8) of the BHC Act (12 U.S.C. § 1843(c)(8)) and section 225.4(b)(2) of the Board's Regulation Y (12 C.F.R. §225.4(b)(2)), to acquire 100% of the voting shares of Fidelity Federal Savings & Loan Association of San Francisco, California ("Fidelity"), and its wholly-owned service corporation. Fidelity is a federally chartered and insured savings and loan association and is the successor by supervisory conversion of Fidelity Savings & Loan Association, San Francisco, California, a California guarantee stock savings and loan association, that was closed by the State of California on April 13, 1982, and placed under the receivership of the Federal Savings and Loan Insurance Corp. ("FSLIC"). (Fidelity is currently operated as a mutual association. In order to effect consummation of the proposal, Fidelity will be converted from a mutual association and issued a charter as a stock federal savings and loan assocaition.)

By letters, dated Aug. 13 and Sept. 8, 1982, the Federal Home Loan Bank Board ("FHLBB") requested that the Board act expeditiously upon this application in light of the emergency nature of the situation at Fidelity and its deteriorating financial condition. In light of this request, the Board promptly published notice of the application in the "Federal Register", providing 21 days for interested persons to comment on the application. In addition, in order to provide a full opportunity for public comment, the Board ordered informal hearings on the application in both Washington, D.C., and San Francisco, California, to receive comments and testimony from interested persons on the application and to allow interested persons to question Citicorp concerning its proposal.

In response to its request for comment on this application, the Board received 35 written comments opposing the acquisition ("protestants") and 11 favoring the acquisition. Ten general comments were received that did not take a position on the proposal. In addition, the Board received sworn testimony from 23 persons who appeared at the two hearings, as well as statements and other documents submitted by the participants at the hearings. As discussed below, a number of protestants requested that the Board order a formal hearing on the application.

The Board has carefully considered the issues raised by the protestants in writing or in oral testimony and, in the appendix attached to this order, which is an integral part hereof, the Board has analyzed these comments and evaluated their relevance to the Board's conclusions in light of the factors set forth in section 4(0)(8) of the BBC Act are elaborated in the appendix. Based upon the record before the Board in this matter, the Board makes the following findings.

Citicorp, with total consolidated assets of $120.1 billion and deposits of $74.5 billion, is the second largest banking organization in United States. (Unless otherwise indicated, all financial data are as of June 30, 1982.) Citicorp operates three subsidiary banks: Citibank, N.A., New York, New York ("Citibank"), the second largest commercial bank in New York with $21.9 billion in domestic deposits, representing 12.3% of the deposits in commercial banks in New York (as of June 30, 1981) Citibank (New York State) NA, Buffalo, New York; and Citibank South Dakota, Sioux Falls, S.D. (Citicorp received Board approval on July 21, 1982, to acquire Citibank (Delaware), Wilmington, Delaware, a proposed new bank. Citicorp. 68 Federal Reserve Bulletin 499 (1982).)

Citicorp also controls numerous nonbanking subsidiaries located throughout the United States, including subsidiaries engaged in consumer lending, mortgage lending mortgage

servicing, industrial banking and commercial lending in California.

Fidelity is a savings and loan association headquartered in San Francisco, California, which operates 81 offices in California, primarily in the San Francisco area, and has regulatory approval for three additional offices. Fidelity, with total assets of $2.9 billion, is the 16th largest savings and loan association in California and the 42d largest in the United States. Fidelity is primarily engaged in taking savings deposits and making loans to individuals secured by mortgages on real property. Fidelity also owns a service corporation that operates in the states of Hawaii and Nevada and that engages in the activities of mortgage lending, real estate development, and the sale and leasing of equipment to Fidelity.

Citicorp's banking subsidaries and Fidelity operate in separate markets. Fidelity operates in 10 California SMSAS, where it controls from 0.24% to 3.7% of the total deposits in commercial banks and savings and loan associations in those markets. (Fidelity's highest market shares of 3.7% is in the Vallejo-Fairfield-Napa SMSA, where it ranks as the sixth largest depository institution.) Citicorp operates approximately 20 offices of its nonbank subsidiaries in California, including industrial loan company offices that engage in limited deposit-taking activities.

Those offices that engage in the same activities as Fidelity have only insignificant market shares and are located primarily in southern California, whereas Fidelity is located primarily in Northern California. For example, in originating first mortgages, Citicorp and Fidelity together account for less than 1.5% of the total volume of mortgages originated in California. Citicorp's share of deposits among all deposit-taking institutions in California is also insignificant.

Citicorp's application to acquire Fidelity was filed and has been considered by the Board under section 4(c)(8) of the BHC Act, which deals with the permissible nonbanking activities of a bank holding company. As explained in the appendix to this order, the Board believes that a federally insured savings and loan association that offers NOW accounts

and that exercises no greater commercial lending powers than are now permitted to federally insured savings and loan association under the Home Owners' Loan Act ("HOLA") is not a bank for purposes of the BBC Act. In this connection, the board also notes that the acquisition and ownership of Fidelity is subject to the Savings and Loan Holding Company Act Act Amendments of 1967 (SELHC Act). Thus the Board concludes that Fidelity is not a "bank" under the BHC Act, that Citicorp's application is properly filed under section 4 of the BHC Act, and that the interstate banking prohibition of section (d) of the BHC Act does not bar Board approval of this application.

Section 4(c) (8) of the BHC authorizes a bank holding company to acquire a nonbank company if the activities of the nonbank company are determined by the Board to be "so closely related to banking or managing or controlling anks as to be proper incident thereto. The Board has determined previously that the operation of a savings and loan association is closely related to banking and reaffirms that determination in this order. (American Fletcher Corp., '60 Federal Reserve Bulletin 868 (1974), D.H. Baldwin & Co., 63 Federal Reserve Bulletin 280 (1977); Interstate Financial Corp., 6B Federal Reserve Bulletin 316 (1982). A recent Board staff study of thrift institutions supports the view that operating a thrift institution is closely related to banking. Bank Holding company acquisitions of Thrift Institutions, September 1981.)

With respect to the proper incident requirement, section 4(c) (8) of the BHC Act requires the Board to consider whether the performance of the activity by an affiliate of a bank holding company "can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gain in efficiency that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, or unsound banking practices."

In 1977, the Board considered the general question whether savings and loan association ("S&L") activities are a proper incident to banking. At that time, the Board determined that, as a general matter, S&L activities were not a

proper incident to banking since the potential adverse effects of generally allowing affiliations of banks and savings and loan associations were then sufficiently strong to outweigh such public benefits as might result in indvidual cases. D.H. Baldwin & Co., 63 Federal Reserve Bulletin 280 (1977).

Because of the considerations elaborated in D.H. Balwin & Co., the Board has not been prepared to permit bank holding companies to acquire thrift institutions on a general basis. However, the Board has consistently regarded the BHC as authorizing the Board to permit such an acquisition. As the problems of the thrift industry began to become more acute in 1981, the Board advised Congress that, in the absence of enactment of emergency thrift acquisition legislation, the public interest might dictate that the Board use its existing authority under BHC Act to approve interindustry acquisitions on a case-by-case basis. The Board indicated that, in the case of a failing thrift institution, any adverse effects of a bank holding company affiliation with a thrift might be overcome by the public benefits associated with preserving the failing institution. In April of this year, the Board approved such an application in order to prevent the failure of a thrift institution.

In a letter, dated Aug. 13, 1982, FHLBB chairman Richard Pratt informed the Board that the FHLBB had selected Citicorp as the winning bidder for Fidelity and urged the Board to act promptly on the Citicorp application in view of the deteriorating financial condition of Fidelity and its continued need for assistance. In a further letter of September 8, 1982 chairman Pratt advised the Board that there is no evidence that the rate of decline in Fidelity's position will slow or that its condition can improve unless it is acquiried by an instiution with greatly superior resources that can rebuild public confidence in the institution.

Fidelity's predecessor will placed in receivership on April 13, 1982, more than five months ago, and Fidelity's condition has steadily deteriorated since that time. Fidelity continues to lose deposits at a rate in excess of $1 million per day and to experience operating losses, estimated at over $200,000 per day. Fidelity has now exhausted its net worth and, as contemplated at the time the FHLBB authorized the FSLIC

to transfer the assets and liabilities of Fidelity's predecessor to Fidelity, Fidelity's net worth will be maintained by advance from the FSLIC, absent consummation of Citicorp's proposal.

In view of the determination by the FHLBB, the primary suervisory authority for Fidelity, with respect to the emergency financial condition at Fidelity, the substantial savings to the FSLIC through the Citicorp proposal, the present curcumstances of the thrift industry and the financial condition of a large number of its members, and the other favorable public benefit considerations listed in the appendix, the Board has determined that consummation of the Citicorp proposal, as specifically conditioned in this order, may reasonably be expected to result in substantial public benefits. These benefits include increased competition and greater convenience to the public through the restoration of Fidelity as an effective competitor and through Citicorp's stated commitments to meet the credit needs of Fidelity's communities. In its evaluation of the public benefits in this case, the Board also has taken into account the beneficial effect on the financial community as a whole of implementing an additional mechanism for the solution of the difficult problems for the thrift industry and the federal insurance funds posed by the poor earnings situation of this industry.

In the exercise of its responsibility under the BHC Act, the Board has carefully considered whether Citicorp's financial and managerial resources are adequate to effect the proposed acquisition of Fidelity. The Board notes that Citicorp has extensive experience in both the consumer banking and consumer finance areas and appears fully capable of revitalizing a consumer-oriented depository institution such as Fidelity. In its evaluation fo Citicorp's financial resources, the Board has reviewed relevant data from Citicorp's inspection reports and the examination reports of its subsidiaries as well as official reports and filings with the Board, including data on Citicorp's loan portfolio.

Based upon this review, the Board concludes that the proposed acquisition would not represent a significant additional burden on Citicorp's financial resources, particularly in view of Fidelity's size in relation to that of Citicorp. Although the

Board has noted, with respect to both Citicorp and other large multinational banks, a long-term trend toward lower capital ratios, the Board also has taken into account as a favorable factor the improvement in Citicorp's capital over the past one and one-half years and recent improvement in its earnings. The Board expects that Citicorp will continue its efforts to improve its capital position and will take such efforts into consideration in acting on applications for further expansion of Citicorp's activities. On balance, the Board concludes that Citicorp has both the financial and managerial resources needed to acquire Fidelity and make it viable competitor without significant adverse effects on Citicorp.

As explained in the appendix, the Board has re-examined, in the context of this application, the general adverse factors cited in the Board's D.H. Baldwin decision, including regulatory conflict, erosion of institutional rivalry and the potential for undermining interstate bank prohibitions, has determined that these adverse effects are outweighed by the substantial public benefits that are expected to result from the restoration of Fidelity as an effective competitor.

In addition, the Board has considered other possible adverse effects that might be associated with this particular application, including the potential for decreased or unfair competition, conflicts of interests, financial risks, diversion of funds, participation in impermissible activities, evasion of interest rate limitations, unsound banking practices, and undue concentration of resources.

In view of Citicorp's limted presence in the relevant California markets served by Fidelity, the number and size of financial organizations operating in these California markets, the legal prohibitions against Citicorp's expansion of its bank subsidiaries into California, and the fact that Fidelity is a failing insitution with limited competitive vigor, the Board concludes that his proposal would not have any significant adverse effects on existing or potential competition in any relevant market. Indeed, the proposed acquisition will have a substantial beneficial impact on competition by insuring the continued operation of Fidelity as a viable institution through access to the financial and managerial resources of Citicorp.

The affiliation of Citicorp and Fidelity also is not likely to result in unfair competition in view of the various conditions imposed by the Board that required Fidelity to be operated independently and not utilized to further or enhance the activities of Citcorp's other subsidiaries. In addition, Fidelity's activities will be limited to those permissible under the BHC Act and its offices will be limited to locations at which banks located in California may extablish branches.

To guard against possible adverse effects of affiliation in this case between a banking organization and a savings and loan association, including the potential for unfair competition and diversion of funds, the Board has established the following conditions for its approval of the application:

1. Citicorp shall operate Fidelity as a federal savings and loan association having as its primary purpose the provision of residential housing credit. Fidelity shall limit its activities to those permitted to federal savings and loan associations currently under the Home Owners' Loan Act and to bank holding companies and their subsidiaries under section 4(c)(8) of the Bank Holding Company Act. These limitations shall apply to Fidelity's wholly owned service corporation, Fidelity Subsidiary Corp., which sall have two years from the date of this order to complete the divestiture of its impermissible real estate development projects.

2. Fidelity shall not establish or operate a remote service unit at any location outside California.

3. Fidelity shall not establish or operate branches at locations not permissible for national or state banks located in California. (The Federal Reserve Bank of New York is hereby delegated authority to act on applications by Citicorp to open additional offices of Fidelity under section 225.4(b)(1) of Regulation Y.)

4. Fidelity shall be operated as a separate, independent, profit-oriented corporate entity and shall not be operated in tandem with any other subsidiary of Citicorp. Citicorp and Fidelity shall limit their operation to effect this condition, and shall observe the following conditions:

a. No banking or other subsidiary of Citicorp shall link its deposit-taking activities to accounts at Fidelity in a sweeping arrangement or similar arrangement.

b. Neither Citicorp nor any of its subsidiaries shall solicit deposits or loans for Fidelity; nor shall Fidelity, directly or indirectly, solicit deposits or loans for any other subsidiary of Citicorp.

To the extent necessary to ensure independent operation of Fidelity and prevent the improper diversion of funds, there shall be not transactions between Fidelity and Citicorp or any of its subsidiaries without the prior approval of the Federal Reserve Bank of New York. This limitation encompasses the transfer, purchase, sale, or loan of any assets or liabilities, but does not include infusions of capital from Citicorp or payment of dividends by Fidelity to Citicorp. (The board does not consider any extension of credit by Citicorp to Fidelity that is necessary to maintain Fidelity's liquidity or general financial integrity to be covered by this limitation.)

6. Citicorp shall not change Fidelity's name to include the work "bank" or any other term that might confuse the public regarding Fidelity's status as a nonbank thrift institution.

7. Fidelity shall not convert its charter to that of a state savings and loan association or other state-chartered thrift institution or to a national or state commercial bank without the board's prior approval.

The board concludes that consumation of the proposal, subject to the conditions set out in this order and the appendix thereto, may not reasonably be expected to result in conflicts of interests, unsound banking practives, undue concentration of resources, or other adverse effects.

The board also has considered the contention that the FSLIC erred in not accepting a bid from one of the California savings and loan associations that bid for Fidelity. The selection of the most favorable bid for Fidelity is a matter committed to the jurisdiction of the FSLIC, and the board concludes that proper administration of the law requires that there should be only one administrative decision on this issue.

The law assigns to the board the responsibility under section 4(c)(8) of the BHC Act for a determination of the public benefits and adverse effects of the application before it—the

Citicorp application—and the board has discharged that responsibility in this order.

Based upon the foregoing and other facts and circumstances reflected in the record and as more fully set forth in the appendix, the board has determined that the acquisition of Fidelity by Citicorp would result in substantial and compelling public benefits that are sufficient to outweigh any adverse effect that may reasonably be expected to result from this proposal, including any potential adverse effects of the affiliation of a commercial banking organization with a thrift institution. Accordingly, the application is approved subject to the conditions and limitations described in this order, the appendix hereto, and the record of this application.

The board has also considered the requests of a number of commenters that the board delay action on the application in order to allow for congressional action on bills now pending before Congress that, if enacted, would establish specific procedures for acquisition of a failing thrift institution by a bank holding company across state lines.

Moreover, the Federal Home Loan Bank Board has advised that the procedures utilized in the Fidelity bidding process generally complied with the terms of these bills; that an extensive attempt, over a long period of time, was made to find interested and capable bidders from within the industry; and that a broad range of bidders, including banks and savings and loan associations, were initially invited to bid, that a rebidding was organized at which California financial institutions were given an opportunity to better or equal Citicorp's bid; and that, accordingly, the basic concepts contained in both versions of these bills were embodied in the procedure by which the FSLIC decided to accept the Citicorp proposal.

In view of these considerations, the board's established legal authority to authorize the acquisition, the request of the FHLBB for expedited treatment of the application in view of the emergency situation of Fidelity, the clear public benefits of the application, and the costs and uncertainties of delay, the board has determined that it would not be in the public interest to delay a decision on the application.

The board has also carefully considered the requests of several protesters that the board hold a formal hearing regarding this proposal. For the reasons specified in the appendix to this order, the board does not believe a formal hearing is required or appropriate in this case and, accordingly, denies the requests of the protesters for a formal hearing.

Several protesters have requested that, in the event the board approves the proposed acquisition, the board stay the effective date of the approval pending judicial review of the board's action. The board has reviewed these requests in light of the factors generally applied by the courts on stay requests and, based upon that review as explained in the appendix to this order, does not believe that a stay of the board's order in this case is appropriate or in the public interest. Accordingly, the board hereby denies protesters' request for a stay of the board's order.

By order of the Board of Governors, effective Sept. 28, 1982.

JAMES MCAFEE
Associate Secretary of the Board

ADDENDUM M

APPENDIX TO FED RULING ON CITICORP ACQUISITION OF FIDELITY

American Banker
October 4, 1982

The following is the appendix to the Federal Reserve Board order approving the acquisition by Citicorp of Fidelity Savings of San Francisco. In the appendix, the Fed addresses the issues raised by the bank holding company's purchase of the savings and loan association. The order itself was published in the Sept. 30 American Banker.

In connection with its decision on the application of Citicorp under section 4(c)(8) of the Bank Holding Company Act to acquire Fidelity Federal Savings & Loan Association of San Francisco, the board issues the following statement containing additional findings of fact and conclusions of law with respect to, and the board's analysis of the issues raised by, the application and the comments received.

(Among the protesters to the application were the Independent Bankers Association of America, the United States League of Savings Associations, the California Bankers Associations, the California Savings and Loan League, and the Conference of State Bank Supervisors. The California financial institutions supervisory authorities also appeared at the informal hearing in San Francisco to express their concerns with the application and to urge delay of any board decision pending congressional action on emergency thrify acquisition legislation. The state representatives expressed concern over the interstate nature of the acquisition as well as the impact it might have on California financial institutions and indicated that the board should hold a formal hearing to explore and evaluate these questions.)

Fidelity's Status as a Nonbank

In its evaluation of the application, the board considered the objections of a number of the protesters that Fidelity should be regarded as a "bank" for purposes of the Bank Holding Company Act; that Citicorp's application to acquire

Fidelity was, therefore, improperly filed under the nonbank provisions of section 4(c)(8) of th BHC Act and should have been filed, and should be considered by the board, under section 3 of the BHC Act, which requires prior board approval before a bank holding company such as Citicorp may acquire control of a bank; and that, because Fidelity is a bank, board approval of its acquisition by an out-of-state bank holding company such as Citicorp is barred by section 3(d) of the BHC Act. (12 U.S.C. §1842(d).)

Section 3(d) prohibits the board from approving an application by a bank holding company to acquire an interest in a bank located outside of the state in which the operations of the bank holding company's subsidiary banks are principally conducted (in Citicorp's case, the state of New York), unless such an acquisition is expressly permitted by the law of the state in which the acquired bank is located.

The BHC Act defines a bank as an institution that accepts deposits that the depositor has a legal right to withdraw on demand and that is engaged in the business of making commercial loans. (12 U.S.C. § 1841 (c))

As a federal savings and loan association, Fidelity is authorized to offer negotiable order of withdrawal accounts and to engage in certain limited commercial lending activities. (12 U.S.C. §§1464(b) and (c) and 1832. Fidelity offers NOW accounts and has outstanding about $190 million in commercial real estate loans, representing about 6% of Fidelity's total assets.)

Based on the terms and legislative history of the BHC Act, the board has previously determined that, because of the checklike powers of NOW accounts and because they generally perform the same function as demand deposits, NOW accounts satisfy the demand deposit test in the definition of "bank" in the BHC Act. (First Bancorp., 68 Federal Reserve Bulletin 253 (1982).)

As indicated, the Board believes that a federally insured savings and loan association that offers NOW accounts and exercises no greater commercial lending powers than are now permitted to a federal savings and loan association under the Home Owners' Loan Act of 1933 as amended is not a "bank" for purposes of the BHC Act. (First Bancorp., 68

Federal Reserve Bulletin 253 (1982); Interstate Financial Corp., 68 Federal Reserve Bulletin 316 (1982). The industrial loan company involved in First Bancorp. offered NOW accounts and made commercial loans in excess of the amount permitted to a federal thrift. Consequently, the board concluded that it was "bank" for purposes fo the BHC Act. On the other hand, the state-chartered and insured savings and loan association in Interstate did not make commercial loans and committed to secure FSLIC insurance, and thus the Board determined that it was not a "bank.")

In reaching this decision, the board has relied on the fact that the lending activities of federal savings and loan associations have historically been highly specialized and, under current statutory and regulatory provisions, continue to be concentrated in home mortgages. The Home Owners' Loan Act expressly provides that the primary purpose of a federally chartered savings and loan association is the provision of residential credit. (12 U.S.C. § 1464. Under the Home Owners' Loan Act, a federal savings and loan association is not permitted to engage in general commercial lending. It may, however, invest up to 20% of its assets in commercial real estate loans and may invest an additional 20% of its assets in commercial paper. 12 U.S.C. § 1464(c)(2)(A) and (B). Fidelity's current loan portfolio appears permissible under the Home Owners' Loan Act.)

In this regard, the board also notes that Congress has designed a separate and independent statutory structure for the regulation of federally insured savings and loan associations and their holding companies. While Congress has recently permitted federal savings and loan associations to engage in limited nonresidential mortgage lending, Congress has left intact a separate statutory and regulatory framework for the operation and ownership of federally insured savings and loan associations and banks.

In the board's view, this provide a strong indication of congressional intent that federally insured savings and loan associations are included within the definition of "thrift institution" under section 2(i) of the BHC Act (12 U.S.C. §1841(i)). This differentiation between banks and thrift institutions in the definitional sections of the BHC Act provides

additional support for the conclusion that federal savings and loan associations that engage in activities no broader than permitted by the terms of the Home Owners' Loan Act are not "banks" within the meaning of the BHC Act. (The board notes that Congress has under consideration legislation that would expand the commercial lending authority of federal savings and loan associations and that would specifically exempt an association exercising such expanded commercial lending authority from the definition of a bank in the BHC Act. S.2879, 97th Cong., 2d Sess. S 333 (1982).

For these reasons, the Board concludes that Fidelity is not a bank under the BHC Act and its acquisition by Citicorp is not barred by section 3(d) of the BHC Act.

(The nonbank provisions of section 4 of the BHC Act do not have an interstate prohibition similar to that in section 3(d) of the BHC Act. Lewis v. BT Investment Managers Inc., 447 U.S. 27 (1980.) There is a provision in the Savings and Loan Holding Company Act that pervents a savings and loan holding company from acquiring an interest in an insured institution that would result in the formation of a multiple savings and loan holding company controlling an "insured institution" in more than one state (12 U.S.C. §1730a(e)(3). Since none of Citicorp's currently-owned bank or nonbank subsidiaries is included within the definition of "insured institution" under the S&L Holding Company Act, the proposed acquisition does not violate this prohibition.

(Several protesters have claimed that Fidelity will be operated as a branch of Citicorp's subsidiary banks and thereby violate the McFadden Act prohibitions against interstate branching (12 U.S.C. §36). The Board has considered this claim and finds that Fidelity will not take deposits or solicit or make loans on behalf of any Citicorp subsidiary bank.

(In addition, Fidelity will be operated separately and independently from Citicorp's bank subsidiaries and, as noted in the order, the board has imposed conditions to ensure such separate operation and to prevent tandem operations.

(On this basis, the board concludes that Fidelity will not be operated as a branch of any Citicorp subsidiary bank and its operation as a subsidiary of Citicorp will not contravene the McFadden Act.)

As noted, the board has required, as a condition of its approval, that Citicorp maintain Fidelity as a federal savings and loan association subject to the restrictions of the Home Owners' Loan Act. An expansion of Fidelity's activities beyond that now permitted to a federal savings and loan association would represent a significant alteration of Fidelity's activities and would require prior board approval under section 225.4(c) of Regulation Y (12 C.F.R. § 225.4(c)).

Closely Related to Banking

Section 4 of the BHC Act generally prohibits a bank holding company from engaging, either directly or through a subsidiary, in nonbanking activities, that is, in activities other than those of banking or managing or controlling banks. (12 U.S.C. §1843 (a)(2)) The principal exception to this prohibition is contained in section 4(c)(8) of the BHC Act, which authorizes a bank holding company to acquire a company engaged in activities that "the board after due notice and opportunity for hearing has determined (by order or regulation) to be so closely related to banking . . . as to be a proper incident hereto. (12 U.S.C. § 1843 (c)(8)) In making the determination of whether an activity is a proper incident to banking, section 4(c)(8) requires that: The Board shall consider whether its performance by an affiliate of a holding company can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, con___ of interests, or unsound banking practices.

Section 4(c)(8) thus requires the board to make two separate findings in order for a nonbanking activity to be permissible for a bank holding company. (National Courier Association v. Board of Governors, 516 F.2d 1229, 1232-1233 (D.C. Cir. 1975).) First, the board must determine whether the activity is "closely related to banking," that is, whether as a general matter the activity is permissible for bank holding companies. Second, the board must determine whether the performance of the proposed activity by an applicant bank holding company may reasonably be expected to produce public benefits that outweigh possible adverse effects.

On a number of occasions over the past 10 years, the board has considered, both in the context of a rule-making proceeding and specific applications, whether the operation of a savings and can association by a bank holding company is a permissible activity for a bank holding company under the close-related and proper incident tests in section 4(c)(8) of the BHC Act. Newport Savings & Loan Association, 58 Federal Reserve Bulletin 313 (1972); American Fletcher Corp., 60 Federal Reserve Bulletin 868 (1974).) In 1974, the board concluded, on the basis of a record compiled after notice and a rulemaking hearing in which numerous parties participated, that the operation of a savings and loan association is closely related to banking within the meaning of section 4(c)(8) of the act.

The board, however, denied the application because the applicant failed to demonstrate that it could satisfy the proper incident to banking test, that is, that the reasonably expected public benefits of the proposal [illegible] weighed possible adverse effects. (In American Fletcher Corp., the board denied on the basis of adverse financial conditions.) In a number of cases decided since that time, the board has consistently held to the position that the operation of a savings and loan association is closely related to banking. (E.g., Memphis Trust Co., 61 Federal Reserve Bulletin 327 (1975); D.H. Baldwin & Co., 63 Federal Reserve Bulletin 280 (1977); Interstate Financial Corp., 68 Federal Reserve Bulletin 316 (1982).)

In this case, the board reaffirms its view as expressed in American Fletcher Corp. and in other decisions that the operation of a savings and loan association is an activity that is closely related to banking. Both banks and savings and loan associations are financial intermediaries with liability structures dominated by loans. The traditional deposit-taking and lending activities of savings and loan associations are functionally and operationally similar to activities performed by banks and require the same type of analysis and expertise.

While the board believes that the operation of a savings and loan association is an activity that is closely related to banking, in order to approve such an activity for a bank holding company, the board must also find that the proposal

meets the proper incident to banking test of section 4(c)(8) of the BHC Act.

Proper Incident to Banking

In 1977, the board considered the general question of whether the operating of a savings and loans association is a proper incident to banking. At that time and on the basis of the factual record presented in that case, the board determined that, as a general matter, such an activity is not a proper incident to banking since the potential adverse effects of allowing affiliations between banks and savings and loan associations on a general basis were sufficiently strong to outweigh the public benefits that might result in individual cases. D.H. Baldwin & Co., 63 Federal Reserve Bulletin 280 (1977).

In the Baldwin case, the board identified three potential adverse effects that could be expected to result from the affiliation of a bank and a savings and loan association: the conflict between the statutory and regulatory frameworks within which banks and savings and loans operate; the erosion of institutional rivalry between banks and savings and loans; and the potential for understanding federal prohibitions against interstate banking.

Based upon competitive considerations and these generalized adverse effects, and in the absence of any compelling public benefits, the board denied the application. In subsequent years, the board approved a number of applications by bank holding companies in New Hampshire to acquire thrift associations but only on the basis of the historical affiliations between banks and thrifts in that state and certain structural and competitive considerations of that affiliation. (E.g., First Financial Group of New Hampshire, 66 Federal Reserve Bulletin 594 (1980). On this same basis, the board had earlier approved applications by bank holding companies to acquire thrifts in the state of Rhode Island. See, e.g.,—Old Colony Cooperative Bank, 58 Federal Reserve Bulletin 417 (1972).)

In 1982, in Interstate Financial Corp., 68 Federal Reserve Bulletin 316 (1982), the board was called upon for the first time to determine whether the adverse effects identified in the Baldwin decision could be offset by the benefits to the

public associated with preserving a financially troubled savings and loan association. In Interstate, the Ohio superintendent of building and loan associations requested the board to consider the application on an expedited basis in view of the facts that the association had nearly depleted its capital and under Ohio law its liquidation would have been required in the near future.

While specifically stating that it did not overrule its conclusion in Baldwin that, as a general matter, the operation of a savings and loan association by a bank holding company is not a proper incident to banking, the board concluded, on the basis of the specific facts in the Interstate case, that the public benefits of preserving the savings and loan association as a viable competitor were so substantial as to outweigh the adverse effects of the interindustry affiliation.

In analyzing the public benefits of the proposal, the board considered the financial conditions facing the thrift industry generally, the financial condition of a number of its members, the lack of any other viable alternative to address the association's financial condition, the request of the Ohio supervisory authorities for prompt action, and the potential ramifications of a liquidation of the association on the association's customers, the depositing public, the state of Ohio, and the Ohio Deposit Guarantee Fund.

D. H. Baldwin Case

In its consideration of the proper incident test in connection with this application, the board has reexamined each of the potential adverse factors found in Baldwin.

With regard to the potential for regulatory conflict, Citicorp is currently a bank holding company and is therefore subject to the provisions of the BHC Act. Fidelity, as a federal savings and loan association, is subject to the provisions of the Home Owners' Loan Act. In order to reduce the potential for conflict between the BHC Act and loan act, the board conditions approval of this application upon Fidelity's activities being limited to those that are permitted both to federal thrift institutions currently under the loan act and to bank holding companies and their nonbank subsidiaries under section 4(c)(8) of the BHC Act. (In the event Fidelity intends to engage, directly or through a service corporation, in any additional nonbanking activity not covered by this application, Citicorp covered by this application, Citicorp and Fidelity would be required to obtain the board's approval under section 4(c)(8) of the BHC Act and section 225.4 of Regulation Y. This application covers the traditional deposit-taking and lending activities of federal savings and loan associations as currently authorized under the loan act, mortgage brokering, loan servicing, and mortgage lending.)

This condition does not limit the performance of the traditional deposit-taking and lending activities of federal savings and loan associations by Fidelity.

(In its D.H. Baldwin decision, the board expressed concern that a condition that limited the activities of a savings and loan association owned by a bank holding company would place the association at a competitive disadvantage and prevent the full realization of public benefits that are expected from the operation of the association. Indeed, the Federal Home Loan Bank Board had opposed the acquisition of a savings and loan by a bank holding company on this basis.

(While the board recognizes that Fidelity's affiliation with Citicorp will limit Fidelity's ability to offer all services authorized under the loan act, the affiliation will restore Fidelity to a viable competitive position and allow it to continue to offer most authorized services. These benefits are, in the board's judgment, more than sufficient to outweigh the fact that Fidelity may no longer engage in real estate development and similar impermissible activities under the BHC Act, activities that represent only a small fraction of Fidelity's overall operations.

(In this regard, Citicorp has indicated it has no desire to engage in such activities but intends to promote Fidelity's basic consumer-oriented services. The board also notes that the FHLBB has urged approval of the application as providing substantial public benefits through the restoration of Fidelity as an active competitor that outweigh any possible adverse effects.)

Upon consummation of the proposal, Citicorp will become a savings and loan holding company under the S&L Holding Company Act. (12 U.S.C. § 1730a.) As a savings and loan

holding company and a bank holding company, Citicorp will be required to conform its activities to the requirements of both statutes.

As a unitary savings and loan holding company, Citicorp is prohibited from engaging in any activity that would have the effect of evading a law or regulation applicable to an insured savings and loan association 12 U.S.C. § 1730a(c)(1). (The FHLBB has granted a waiver to Citicorp of the restrictions on the amount of debt that can be incurred by a nondiversified savings and loan holding company (12 U.S.C. § 1730a-(g)).

In the board's view, Citicorp will be able to continue its bank holding company and commercial bank operations without conflict with the S&L Holding Company Act or the Home Owners' Loan Act.

In view of the above, the board concludes that while some adverse consequences may result because of regulatory conflicts between the BHC Act, the Home Owners' Loan Act, and the S&L HC Act, these adverse effects are mitigated by the conditions imposed in this order to require Citicorp's compliance with the terms of each statute and, as discussed below, to prevent any unfair competitive advantage accruing to Citicorp or Fidelity by reason of the affiliation.

The board also continues to believe that, as a general matter, the affiliation between banks and thrifts may produce possible adverse effects by diminishing the interindustry rivalry that has produced price and service benefits to the public and by undermining the prohibition of the BHC Act against interstate banking. However, these adverse effects, in the context of this case, are substantially mitigated by the fact that Fidelity is a failing institution that has lost its competitive vigor and is able to continue operations only through substantial federal financial assistance.

As discussed below, the board believes that the revitalization of and restoration of public confidence in Fidelity is a public benefit that, along with other public benefits, outweighs any adverse effects that may result from consummation of the proposal.

Moreover, to ameliorate further the possibie adverse effects of affiliation in this case between a banking organization and a thrift association, the board has conditioned approval of the proposal to require that Fidelity continue to be operated as a savings and loan association having as its primary purpose the provision of residential credit, that its offices be confined to California, and that Fidelity and Citicorp's subsidiaries be operated separately and independently of one another. The board believes that such restrictions will minimize the potential for erosion of statutory prohibitions against interstate banking and maintain the independence and specialized function of the savings and loan industry.

Other Possible Adverse Effects

As discussed below, the board in its evaluation of the application has also considered the potential for additional adverse effects that might result from consummation of Citicorp's particular proposal, including the potential for decreased or unfair competition, conflicts of interest, financial risks, diversion of funds, participation in impermissible nonbanking activities, evasion of interest-rate limitations, and undue concentration of resources.

In this connection, the board considered the contentions of the protesters that, in addition to the general effects cited by the board in Baldwin, the following addverse effects may result from consummation of the Citicorp proposal: (1) The acquisition would result in a major restructuring of the financial services industry, and Citicorp would obtain an unfair competitive advantage over commercial banks andd thrift organizations that are not afforded the combination in one organization of thrift and commercial banking powers; (2) decreased or unfair competition would result because Citicorp's substantial resources would enable it to strengthen the competitive position of Fidelity to the detriment of the already weakened thrift industry in California; (3) Citicorp would operate Fidelity in tandem with its banking and other subsidiaries through the use of Fidelity's deposits to fund Citicorp's other activities or through the use of Citicorp's other subsidiaries to attract deposits to Fidelity; (4) Citicorp may not have the financial ability and resources to operate and revitalize Fidelity; and (5) the transaction would result in an undue concentration of resources.

Protesters also allege that other adverse considerations warrant denial of Citicorp's proposal, namely, (1) the procedures utilized by the FSLIC in the bidding process for Fidelity were unfair, and the Citicorp offer for Fidelity was not the offer most favorable to the FSLIC and the public; (2) no emergency situation exists at Fidelity in that it is no longer a failing institution now that it is under FSLIC receivership; and (3) the Citicorp proposal is not the only available alternative to address Fidelity's situation and thus does not qualify for approval under the criteria cited by the board in its Interstate decision.

Unfair Competition

The board does not believe that the evidence of record in this case supports the proposition that the acquisition would result in a major restructuring of the financial services industry. On the contrary, the board believes that the proposed acquisition, in light of Citicorp's commitments and the conditions imposed by the board in this order, will result in the operation of two independent and different types of depository institutions supported by the financial and managerial strength of a parent holding company that will permit these organizations to provide substantial public benefits in their respective product and geographic markets.

Citicorp has filed an application to acquire and operate a savings and loan association in California and has stated that it will operate Fidelity independently of its commercial banking activities.

The board has considered the application only on the basis and its approval as conditioned by this order is designed to ensure that Fidelity will be operated as a savings and loan association and will continue to serve the specialized purpose for which it was organized and will not be utilized to further or enhance the activities of Citicorp's subsidiary banks.

The board has given careful consideration to the contention that Citicorp will obtain an unfair competitive advantage over commercial banks through affiliation with a savings and loan association that may engage in activities that are not authorized for banks e.g., certain service corporation activities).

To address these concerns, the board has limited Fidelity activities to those permissible for bank holding companies under the BHC Act and to locations at which banks located in California could establish branches. As the board has previously held, the BHC Act requires that the activities of a thrift institution that is acquired by a bank holding company must be limited to those permissible under the BBC Act.

Activity Limited

In conformance with that holding the board's approval of this application does not authorize Citicorp to engage in any activity through Fidelity that is not permissible under section 4(c)(8) of the BHC Act.

(This requirement is also applicable to activities performed by Fidelity through a service corporation. The board has previously held that, under the BBC Act, a bank holding company subsidiary may not perform indirectly through a service corporation an activity that is impermissible for the bank holding company. Fidelity's service corporation, therefore, must terminate all activities that are not permissile under the BHC Act.)

(Fidelity currently is engaged, through its service corporation, in a number of real estate development projects, an activity that is not permissible for a bank holding company. In accordance with Citicorp's commitments and the terms of this order, Fidelity may not engage in any additional real estate development projects either directly or through a service corporation. In order to afford Fidelity a reasonable period of time to divest currently held impermissible assets and in view of the fact that such assets consist primarily of real estate projects, the board has provided a two-year divestiture period for such assets.)

In addition, this order does not authorize Fidelity to perform any activity that is not permitted to a federal savings and loan association under the HOLA. As a condition of this order, Fidelity may not, without specific approval by the Board, exercise any deposit-taking or commercial landing powers not currently authorized by statute for a federal savings and loan association.

Branching Limitations

Finally, in order to prevent Citicorp from securing any competitive advantage with regard to geographic location over commercial banking organizations operating in California, the board's approval is conditioned upon applicant not establishing branches of Fidelity at locations not permissile for national or state banks located in California.

In order to prevent any unfair competitive advantage that might result from Fidelity's ability to establish remote service units in other states, the board also conditions approval upon applicant not establishing or operating a remote service unit at any location outside of California. The board believes that these restrictions are consistent with Citicorp's statements to the board that Citicorp intends to operate Fidelity as a savings and loan association in California and does not intend to use Fielity to achieve interstate branching or interstate acquisitions or to attract deposits from Citicorp's New York customers or from anywhere else in the country outside of California.

As noted in the order, to further ensure that Fidelity is operated as a savings and loan association and not utilized to further or enhance the activities of any Citicorp subsidiary, the board has imposed the conditions that require Fidelity to be operated as a separate, independent, profit-oriented corporate entity and has prohibited Fidelity from be operated in tandem with any other subsidiary of Citicorp.

(The board has previously indicated that serious adverse effects, including the potential for conflicts of interest, unfair competition and evasion of federal interest-rate limitations, may result from the tandem operation of a bank and a thirft association. First Financial Group of New Hampshire Inc., 66 Federal Reserve Bulletin 594 (1980), Heritage Banks Inc., 66 Federal Reserve Bulletin 590 (1980).)

Prohibit Certain Transactions

The board has also prohibited certain transactions between Fidelity and Citicorp or any of its subsidiaries without the board's prior approval. While the board has prohibited Citicorp from changing Fidelity's name to include the word "bank" or an other form that might confuse the public re-

garding Fidelity's status as a nonbank thrift institution, the Board does not regard as unfair competition applicant's use of the "Citi" prefix or the name "Citicorp" in Fidelity's name.

The board believes these conditions also address the concerns raised by several of the protestants regarding the potential for diversion of Fidelity's funds by Citicorp.

The potential adverse effects that might result from shifting assets and liabilities between Fidelity and Citicorp's other subsidiaries to take advantage of differing interest rates and costs is further protected against through the restrictions on interaffiliate transactions imposed by the Federal Reserve Act.

(Fidelity is subject to interest rate ceilings under 12 C.F.R. Part 526.)

Financial Support

The board has also considered the contention that Citicorp's financial support for Fidelity will give Fidelity an unfair competitive advantage over its thrift competitors.

In the board's opinion, the restoration of Fidelity as a viable competitor and the increased competition and improved and expanded services that are expected of Fidelity through access to the financial and managerial resources of Citicorp may only be viewed as a public benefit. (The fact that Citicorp will receive assistance from the FSLIC also will not result in unfair competition. According to the FSLIC, the Citicorp proposal in fact entails less financial assistance than the proposal of any other bidder. However, even if this were not the case, the FSLIC assistance merely remedies the severe competitive disadvantage now affecting Fidelity as a result of its weak financial condition.)

The fact that a particular depository institution is owned by an organization that is able to provide it with financial and managerial assistance may provide the institution with a competitive advantage, but there is nothing unfair about such an advantage. (The board also notes that a number of other thrift institutions in California are owned by parent organizations that are able to provide their subsidiaries with substantial financial support.)

Indeed, one of the principal concerns of the board under the BHC Act is that a bank holding company should serve as a source of financial strength and support for its subsidiaries.

Finally, the restrictions imposed in this order that Fidelity be operated as a separate, profit-oriented savings and loan association will also protect against unfair competition by Fidelity through its affiliation with Citicorp.

Case-by-Case Approach

The board also has considered the contention that the board's limitation of thrift acquisitions by bank holding companies to situations involving a failing institution and its case-by-case approach to such situations creates an unfair competitive situation. (The board notes that none of the protestants stated that it had been prevented from submitting an offer to acquire Fidelity were afforded a second opportunity to meet or exceed the Citicorp bid. In any event, the federal deposit insurance agencies have traditionally limited the group of institutions from which bids are solicited to ensure an orderly and prompt resolution of an emergency situations and this matter is appropriately reserved to the discretion of these agencies.) The board's approach to the question of thrift acquisition by bank holding companies is mandated by the BBC Act.

Where the board finds adverse a facts associated with a bank holding company proposal, the board is precluded from approving the proposal in the absence of counter-vailing public benefits. Because of the adverse effects associated with the affiliation of banks and thrifts that were identified by the board in "Baldwin," the board may only approve such an application where public benefits are present on the facts in a particular case that outweigh adverse effects. Such compelling public benefits have only been found where the thrift institution is failing.

Undue Concentration of Resources

The board has considered whether the proposal will result in an undue concentration of resources. Citicorp is the second largest banking organization in the country on the basis of total assets. Citicorp controls about 1.29% of domestic deposits in commercial banks, and savings and loan associations in the United States. On this basis, Citicorp is the third largest financial institution in the United States. Upon consummation, Citicorp would control approximately 1.37% of deposits in such institutions and would remain the third largest institution on this basis. The acquisition would increases Citicorp's total assets by 2.5%. Fidelity is the 42nd largest savings and loan association in the United States, and is not viewed by the Board as a predominant firm in its industry or in any geographic market. On the basis or ___ facts and in view of Fidelity's financial condition, the board concludes that consummation of the proposal will not result in an undue concentration of resources.

The board concludes that concludes at consummation of the proposal, subject to the conditions set out in this order, may not reasonably by expected a result in conflicts of interest, unsound banking practices, or other adverse effects.

In reaching the conclusion that consummation of the proposal would not have a substantial impact on Citicorp's overall financial positions and the Citicorp has both the financial and managerial resources needed to acquire Fidelity and make it a viable competitor without any significant adverse effects on Citicorp, the board has considered the comments of the IBAA, the U.S. League, and others regarding Citicorp's foreign loan portfolio.)

Reasonably Expected Public Benefits

The board has also examined the record to determine whether consummation of the proposal may reasonably be expected to produce public benefits. The board believes that Citicorp's acquisition of Fidelity will provide a substantial and compelling public benefit in that Citicorp will provide Fidelity with sufficient new capital funds and managerial assistance to restore Fidelity as a viable competitor and to restore public confidence in Fidelity. Fidelity is a substantial organization, serving thousands of customers in numerous communities. In the board's opinion, the public benefits generally associated with revitalization of a failing financial institution are magnified in this case in view Fidelity's size and the number of its customers.

Restore Active Competitor

The record establihes that Citicorp has the financial and managerial resources and the commitment to serving the convenience and needs of the public to achieve this result. The acquisition will restore an active and effective competitor to, and increase competition in, numerous California markets, presents the potential for expansion and increased competition in other California markets, ensures the continuation of services by Fidelity to its customers and the public and protects the interest of Fidelity's depositors, the public, the savings and loan industry generally, and the FSLIC.

(In this connection, the U.S. Department of Justice stated that the acquisiton of thrift institutions by bank holding companies is procompetitive and will provide enhanced services at competitive prices, similarly, the Comptroller of the Currency urged approval of the proposed acquisition on the basis that it would be procompetitive and would provide significant public benefits.)

(The comptroller also expressed the view that the cost savings to the FSLIC would be a public benefit to other FSLIC-insured institutions and their depositors in view of the potentially large liabilities of the FSLIC as a result of the financial condition of the thrift industry. The Federal Deposit Insurance Corp. took no position on this particular application but stated its belief that the board has discretion under the BHC Act to approve the acquisition by a bank holding company of a thrift and that such an acquisition would provide an additional alternative for resolving situations involving financially troubled financial institutions and would be in the public interest.)

The board has considered as a substantial public benefit the savings to the FSLIC that will result from the proposal. The FHLBB has advised the board that the Citicorp bid was $143 million more favorable to FSLIC than any other bid received and $303 million less than the cost of maintaining a phoenix association. The FHLBB has also advised the board that, using an optimistic projection of interest rates, Citicorp's bid was $56 million more favorable than the next lowest second round bid and $35 million less than the cost of maintaining a phoenix association.

Citicorp's commitment to the introduction of new products and services and the expansion of current services and the expansion of current services of Fidelity through access to Citicorp's financial and managerial resources also lends weight toward approval.

Substantial Public Benefits

In addition to the substantial public benefits associated with the revitalization of Fidelity that have already been cited, Citcorp has stated that it intends not only to restore Fidelity as a competitor but to enhance its competitive position and to promote its services to the public by providing Fidelity with access to resources for the expansion of services in the areas of NOW accounts, consumer loans, credit cards, education loans, trust activities, and automated teller facilities.

This expansion of Fidelity's services and operations also will provide greater convenience to the public. Citicorp's experience and expertise, particularly in managing large scale operations and in the design and implementation of electronic banking and financial data processing, also should provide gains efficiency at Fidelity.

Finally, Citicorp has a good record of service to the convenience and needs of the public and has stated that it intends to use its resources to promote and expand Fidelity's service to its communities, including services directed to the credit needs of low- and moderate-income neighborhoods in those communities. (While the board does not believe that the Community Reinvestment Act is applicable in the case of section 4 applications, the board has considered Citicorp's record under that statute in acting upon this application.)

Community Consultation

In this connection, Citicorp representatives testified at the informal hearings that Fidelity would consult with community groups to determine the credit needs of the community and would study complaints with respect to Fidelity's lending and correct any deficiencies. The Board expects that Citicorp will adhere strictly to these commitments.

As stated above, protesters have asserted that Fidelity should not be regarded as failing institution because its con-

dition has stabilized as a result of the FSLIC receivership. According to protesters, this FSLIC assistance could continue for some time without significant deterioration in Fidelity's condition. Similarly, protesters state that declining interest rates have reduced funding costs for Fidelity and this also has served to relieve pressure on the institution.

The board concludes that any realistic assessment of Fidelity's condition compels the conclusion that Fidelity is a failing institution.

—— and Borrowings

It is undisputed that, on April 13, 1982, following a period of substantial deposit losses and substantial borrowings from the Federal Home Loan Bank of San Francisco of approximately $1.4 illion to maintain liquidity, the California Savings and Loan Commissioner closed Fidelity's predecessor and appointed the FSLIC as receiver for the state on the basis that Fidelity's predecessor was in an unsafe condition and conducting its business in an unsafe and injurious manner.

Substantial operating losses have continued at Fidelity since the receivership was announced and Fidelity's approximately $2.9 billion in assets is now supported by loans from the Home Loan Bank of over $1.7 billion. Deposit withdrawals at Fidelity have also been steady and substantial since appointment of the FSLIC as receiver and have forced the FSLIC to guarantee an advance of an additional $325 million to Fidelity from the Home Loan Bank since April 13.

The FHLBB has provided the Board —h data indicating that deposit outflows at Fidelity have increased during the first 21 days of September. The FHLBB has also advised that Fidelity's operating losses continue substantially unabated and that Fidelity has exhausted its net worth.

Much of the market value of a depository institution such as Fidelity is derived from its deposit base. More than 20% of Fidelity's deposit base has been dissipated since March 31, and thus, the assets held by the FSLIC as receiver must be regarded as wasting.

In addition, advances from the Home Loan Bank have grown to the point that they exceed Fidelity's deposits by a considerable margin. The FHLBB has informed the board that these advances now represent by far the greatest ratio

of advances to savings of any federally insured thrift institution.

The lack of public confidence in Fidelity even after the creation of the FSLIC receivership supports, in the board's view, the statement of the FHLBB that there is no evidence that the rate of decline in Fidelity's revitalization and rebuild public confidence in Fidelity. (Such an acqusition is also necessary to prevent the loss of employees that Fidelity is experiencing. The current receivership cannot provide the stability needed to retain key employees. Delay in resolving Fidelity's problems would mean that even greater efforts would be required to rebuild both employee morale and public confidence.)

In this regard, the FHLBB has advised the board that Fidelity's acquisition by Citicorp would make Fidelity viable again and remove any future risk that extraordinary assistance by the FSLIC would be needed.

Action to Minimize FSLIC Loss

For these reasons, the board concludes that Fidelity's continuing and unresolved financial problems require prompt action to minimize the loss to the FSLIC and provide Fidelity with a strong parent organization capable of restoring public confidence in that institution.

In the board's judgment and in light of the commitments made by Citicorp and the conditions imposed in this order, the public benefits expected from the restoration of public confidence in Fidelity and in the savings and loan industry, the substantial savings to the FSLIC, and reasonably expected gains in efficiency, increased competition and greater convenience to the public, outweigh any adverse effects that are associated with this proposal.

FSLIC Bid Procedures

Protesters have also asserted that, contrary to the determination by the FSLIC, Citicorp's bid to acquire Fidelity would not in fact result in the lowest cost to the FSLIC and that the FSLIC erred in not accepting a bid from one of the savings and loan associations that bid for Fidelity. The board does not believe that this is a proper issue for resolution by the board under section 4(c)(8) of the BHC Act. (The board

has considered the contention that the FSLIC is not authorized to sell the assets held by Fidelity because of litigation pending regarding the appointment by the FHLBB of the FSLIC as federal receiver. Fidelity Savings and Loan Association v. FHLBB, et al., No. 82-4337 and 82-4354 (N.D. Calif.). The board notes that the appointment of the FSLIC as receiver has not been stayed or otherwise enjoined and its appointment as receiver is, therefore, valid at this time. Nor has the court enjoined the FSLIC from transferring Fidelity to Citicorp.)

Section 4(c)(8) of the BHC Act does not require a determination that a given proposal is the most desirable that could be presented. Rather, the statute directs the board to determine whether reasonably expected public benefits from any given proposal outweigh possible adverse effects. The fact that alternative purchasers may be available is not determinative.

Even if the board were to conclude that another bid should have been accepted by the FSLIC, this decision would have little meaning because the board has no authority to award the right to acquire Fidelity to another bidder.

The decision as to which bid to accept is committed to the exclusive discretion of the FSLIC. An orderly administrative process dictates that the board substitute its judgment for that of the FSLIC. The board does, however, note that the procedures followed by the FSLIC generally complied with the procedures now under consideration by Congress for acquisition of failing federally insured thrift institutions and that FSLIC's decision to allow a second round of bidding for Fidelity in order to provide California financial organizations with an opportunity to match the bid of Citicorp adhered to the spirit of these proposals. The FSLIC also published the procedures it followed to the second round bidding in the Federal Register (47 Fed. Reg. 31322 (1982)).

Alternatives to Citicorp Proposal

A number of the protesters argued that the board's authority to approve a failing thrift acquisition under the BHC Act is limited to the situation presented in the Interstate case, where the Bard found that one of the factors in favor of

approval was the fact that the bank holding company's proposed acquisition was the only available means by which the thrift institution could be maintained as a competitor and prevented from being liquidated.

The fact that the proposed bank holding company acquisition of the thrift association in Interstate was the only available means of dealing with its condition was only one of the considerations that the board took into account in approving the Interstate application. There is no legal requirement under the BHC Act that there be no other viable alternative to a bank holding company acquisition of a failing thrift, and there is no indication in its Interstate decision that the Board intended that this factor must be present in every bank holding company application to acquire a failing thrift. (The approval of the primary regulatory authority for an acquisition of a failing thrift association is also not requirement under section 4(c)(8) of the BHC Act. In any event, in this case, the primary regulatory, the FHLBB, has urged board approval of the application as a means of restoring Fidelity to a stable condition.)

As was the case in Interstate, the primary regulator for Fidelity has explored all of the alternatives and has determined that the Citicorp proposal is substantially more favorable to Fidelity, its depositors and creditors and the FSLIC than any other bid and substantially reduces the insurance liability and risk to the FSLIC, including the potential cost, as compared to any other bid. The presence or absence of alternatives is but one factor in the evaluation of public benefits. As indicated, the board's responsibility under the BHC Act is to balance public benefits against possible adverse effects. In this case, the board believes that the balance of public benefits is favorable and that the application may be approved.

Several of protesters (including the IBAA, the U.S. League, the California ___ers, Crocker National Bank, Fidelity Federal Savings and Loan Association, Glendale, Calif., the California supervisory authorities, and Option Advisory Services Inc.) have requested the board to hold a formal hearing regarding Citicorp's proposal. They raise as the basis for a hearing the following:

(1) discovering is necessary so that all relevant facts associated with the application, including the complete record of the FSLIC's consideration of rious bids, may be provided to protesters;

(2) the need to "probe" or "examine" whether Citicorp has the fnancial resources to operate Fidelity in light of current international economic conditions;

(3) the need to assess the policy plications of Citicorp's application had the competitive effects of the proposal on banks and thrifts in California and the nation;

(4) whether Fidelity is or will be operated as a bank and whether its acquisition violates section 3(d) of the BHC Act;

(5) whether Citicorp's bid was more favorable than any other bid; and

(6) whether Fidelity's financial condition is so serious as to warrant Board approval of this application.

Both the board's rules of procedure and the Federal Register notice regarding this application state that any request for a formal hearing must indicate why a written proceeding would not suffice in lieu of a formal hearing and identify the disputed issues of fact that would be resolved at the formal hearing.

The persons requesting a hearing did not comply with this procedure. Rather, the hearing requests were conclusory in nature, did not delineate specific disputed facts, and were based on issues derived from the conclusions to be drawn from undisputed facts.

Apart from the fact that the protesters did not comply with the board's regulations and its notice, the protesters also failed to raise any factual issues that would warrant a hearing. With respect to the FSLIC bid procedures, the board believes that the issue of which bid was the more favorable and the fairness of FSLIC's procedures are not relevant to this proceeding and, thus, a hearing on these issues is not warranted.

Fidelity's Status

The question raised concerning Fidelity's status under the BHC Act involves an issue of law that also does not require a hearing. There is no dispute that Fidelity offers NOW accounts and makes commercial real estate loans in accordance with the provisions of the HOLA.

Assessment of the quality of Citicorp's or Citibank's loan portfolio and Citicorp's financial ability to operate Fidelity is a responsibility that is vested in the federal bank regulatory agencies, and public participation in this process would be inconsistent with the entire scheme of federal bank regulation.

The board's assessment under the BHC Act of Citicorp's financial resources, including its overseas loan portfolio, is based upon detailed examination of the operations of Citicorp's subsidiaries. Protesters have alleged no dispute as to the facts regarding Citicorp's financial resources or its foreign loans, but rather have merely advanced conjectural and conclusory statements to support their hearing request on this point.

Indeed, the hearing requests are framed in terms of a need to probe or examine rather than on any specific or supported allegation of financial weakness.

In the board's opinion, protesters' questions regarding Citicorp's financial resources and the conclusions to be drawn therefrom do not require a formal hearing. Protesters were afforded ample opportunity to present their testimony on these points and to question Citicorp. To warrant a hearing, the board believes that protesters must raise more than generalized claims and requests to "probe" an applicant's financial resources.

In the board's opinion, the hearing requirement in the BHC Act, as it has been interpreted by the courts, does not require the Board to hold a hearing on the basis of conjecture or unsupported allegations and the board is not required "to investigate every potential adverse contingency which a contestant hypothesizes."

Unfair Competition Concern

The essential element of protesters claim of unfair competition is a request that the board evaluate the competitive impact of the proposal based on the allegation that Citicorp would be an effective and aggressive competitor with advantages not available to its banking and thrift competitors. As

explained above, the board believes it has addressed these concerns through the imposition of appropriate conditions that eliminate the unfair competitive advantage that the protestants claim may result, and in any event material facts are not in issue regarding the allegation of unfair competition.

The board believes that the procedures it used to solicit and explore the various policy and legislative-type concerns raised by protestants were appropriate under the circumstances and fully adequate under the BHC Act. The board imposed no limitation on the length or nature of the written comments.

In addition, the board held informal hearings in Washington, D.C., and San Francisco, Calif. that were attended by a total of approximately 200 people. All persons that wished to speak at these hearings were given an opportunity to do so, and all persons that spoke at the informal hearings were given an opportunity to submit questions to Citicorp regarding the application. A member of such questions were received and Citicorp responded to all of them.

In addition, the board has explored the policy issues raised by protesters on a number of occasions over the last ten years, including in a rulemaking proceeding and oral presentation to the board. Last year, the board's staff completed a detailed study of the implications of thrift acquisitions by bank holding companies. The board solicited public comment on the general issue of such acquisitions in conjunction with this study and reviewed some 379 written comments on that study.

No Formal Hearing Needed

Based on the foregoing considerations, the board does not believe that a formal hearing is required or appropriate in this case and denies the requests of the protestants for a formal hearing.

(The board provided 21-days notice in the Federal Register of receipt of Citicorp's application to acquire Fidelity. Since the Federal Register Act states that a statutory requirement of notice and opportunity for hearing is satisfied by a notice period of fifteen days (44 U.S.C. § 1508), the board believes that the notice period in this case is legally sufficient. The board also believes that the twenty-one day comment period is appropriate in view of the request of the FHLBB that the board act expeditiously and the fact the board also held two informal hearings at which interested persons could provide comments on the application and question Citicorp concerning the proposal. The board believes that interested persons have been afforded ample opportunity under the circumstances to submit their views on the proposal.)

Request for a Stay of the Order

Several protesters, including the IBAA, have requested that, in the event the board approves the proposed acquisition, the board stay the effectiveness of the approval pending judicial review of the board's action. The board has reviewed these requests in light of the factors generally applied by the courts on stay requests and, based upon that review, does not believe that a stay of the board's order in this case is appropriate.

First, as explained in detail above, the board believes that its approval of Citicorp's acquisition of Fidelity, subject to the conditions imposed in the order, complies with all applicable procedural and substantive requirements and is supported by substantial evidence. Accordingly, it is unlikely, in the board's opinion, that any protesters will be successful in overturning the board's approval on judicial review.

Second, the board has expressly found that Citicorp's acquisition of Fidelity is not likely, under the conditions imposed by the board, to result in any significant unfair competitive advantage, or other competitive harm to depository institutions that compete with Fidelity or Citicorp, or to their depositors, or the public generally. Moreover, in this case, there is little likelihood that consummation of the acquisition would prevent a reversal of the transaction should such action subsequently become necessary since Fidelity will be maintained as a separate corporate entity. Thus, in the board's view, there is no likelihood of any irreparable harm to any protesters if a stay is not granted.

Third, the board has found that, in light of Fidelity's significant continuing daily net loss of deposits and its operating losses, a delay in consummation of this proposal would permit continued significant financial harm to Fidelity that would otherwise be remedied by consummation of the proposal. Moreover, delay would continue to encourage the departure of employees and to exacerbate the adverse publicity regarding Fidelity since its closing by supervisory authorities. Because of these facts, the board is concerned that it may be more difficult to restore Fidelity to a viable condition if a stay is granted.

The loss of Fidelity's important competitive presence would harm the customers for financial services in its market area. Citicorp would also be harmed by a stay pending review since delay would increase significantly the amount of funds Citicorp would be required to expend to revitalize Fidelity. Finally, during the pendency of any stay, the FSLIC, as receiver of Fidelity, may be required to extend funds to Fidelity to cover its continuing operating losses and to assure maintenance of some minimal net worth, funds that could be used to assist other financially troubled institutions.

The board finds, therefore, that the granting of stay would cause significant harm to third parties.

Finally, the board believes that a stay in this case is clearly not in the public interest. A stay would leave unresolved for a lengthy time the ultimate control and ownership of a failing thrift institution, would prevent the restoration of Fidelity as an active competitive force in its market area, and could result in substantial losses to the FSLIC.

For these reasons, the board hereby denies protesters' request for a stay of the board's order.

Conditions of Approval

The board's approval of this application is further subject to the conditions set forth in section 225.4(c) of Regulation Y and to the board's authority to require such modification or termination of the activities of a holding company or any of its subsidiaries as the board finds necessary to assure compliance with the provisions and purposes of the BHC Act and the board's regulation and orders issued thereunder, or to prevent evasion thereof.

The transaction shall be made not later than three months after the effective date of this order, unless that period is extended for good cause by the board or by the Federal Reserve Bank of New York acting pursuant to authority hereby delegated.

By order of the board of governors, effective Sept. 28, 1982. (Voting for this action: Chairman Volcker and governors Martin, Partee, Teeters, Rice, and Gramley. Absent and not voting: governor Wallich.)

James McAfee
Associate Secretary of the Board

EDITOR'S NOTE

THE FOLLOWING PAGES WERE POOR HARD COPY AT THE TIME OF FILMING. IF AND WHEN A BETTER COPY CAN BE OBTAINED, A NEW FICHE WILL BE ISSUED.

Interstate Banking: Taking Inventory

U.S. banking organizations now control over 7,000 interstate offices. Even if present prohibitions are lifted, however, the evidence suggests that interstate bank expansion will evolve slowly and will be limited to the more attractive markets.

Although interstate banking is prohibited by the McFadden Act and the Douglas amendment to the Bank Holding Company Act, the fact is that banking organizations are providing financial services across state lines and have been doing so for some time. Four gateways allow commercial banking organizations to offer financial services on an interstate basis. First, "grandfather" provisions of banking legislation allow some banking organizations to maintain full-service commercial banks in more than one state. Second, the Garn-St Germain Depository Institutions Act of 1982 allows banks and savings and loan associations to acquire failing institutions across state lines. Third, and perhaps more importantly, the 4(c)8 provisions of the Bank Holding Company Act allow bank holding companies to establish or acquire nonbank subsidiaries that are not subject to the prohibitions on interstate banking. And fourth, other nonbank subsidiaries may establish offices across state lines, i.e. loan production offices and Edge Act corporations, allowing their parent organization to provide financial services on an interstate basis.

In addition, the BHC Act allows bank holding companies to acquire or establish banking subsidiaries in states which explicitly permit such entry. This article will describe various ways in which bank holding companies provide interstate financial services and will inventory their activities on a state-by-state basis. This should give us some idea of the extent to which bank holding companies are actively supplying interstate financial services. The numbers presented in this inventory represent the best available information but may not include all activities or offices. Therefore, the figures represent activities and offices documented by our inventory and should be viewed as a minimum.

Grandfathered Interstate Banking

Legislation and regulation tend to follow actual events in the marketplace. This is especially

1014 YY

Table 1. Foreign and Domestic Bank Holding Companies With Subsidiary Banks In More Than One State

Bank Holding Company	Home State	Number of States	States In Which Banks Are Located
First Interstate Bancorporation	CA	11	AZ, CA, CO, ID, MT, NM, OR, NV, WA WY, UT
First Bank System, Inc	MN	5	MN, MT, ND, SD, WI
Northwest Bancorporation	MN	7	IA, MN, MT, NE, ND, SD, WI
Otto Bremer Foundation	MN	3	MN, ND, WI
Financial General Bancshares, Inc	DC	5	DC, MD, NY, TN, VA
General Bancshares Corporation	MO	3	IL, MO TN
First Security Corporation	UT	3	ID, WY, UT
Citicorp	NY	3	DE, NY, SD
Bank of Montreal*	NY	2	CA, NY
Canadian Imperial Bank of Commerce*	NY	2	CA, NY
The Bank of Tokyo, Ltd*	CA	2	CA, NY
Barclays Bank Limited*	NY	2	CA, NY
The Sumitomo Bank, ltd.*	CA	2	CA, HI
The Royal Bank of Canada*	NY	2	NY, PR
Banco Central, S.A.*	NY	2	NY, PR
J.P. Morgan & Company	NY	2	DE, NY
The Girard Company	PA	2	DE, PA
NCNB Corporation	NC	2	FL, NC
Chase Manhattan Corporation	NY	2	DE, NY
Provident National Corporation	PA	2	DE, PA
Northern Trust Corporation	IL	2	FL, IL
Maryland National Corporation	MD	2	DE, MD
Philadelphia National Corporation	PA	2	DE, PA
First Maryland Bancorp	MD	2	DE, MD
Equitable Bancorporation	MD	2	DE, MD
Chemical New York Corporation	NY	2	DE, NY
Manufacturers Hanover Corporation	NY	2	DE, NY
Pittsburg National Corporation	PA	2	DE, PA

Source: Federal Reserve Board as of 12/31/82
*Foreign banking organizations

true in banking. Market participants first become creative in terms of supplying financial services, and then legislators and regulators react to the evolving market circumstance. Reacting to changing market conditions means that legislators are constantly faced with restricting given activities after innovative organizations have engaged in the activity. In some cases it would be detrimental or impossible to require the organization to cease the activity even though a general prohibition is deemed desirable. In such cases, one equitable approach is to allow the innovative organization to continue but not expand the activity in question. Such a clause is then written into the legislation and is termed a "grandfather provision." A number of domestic and international banking organizations enjoy such grandfather provisions with respect to prohibitions on interstate banking.

We were able to identify 21 domestic bank holding companies that controlled banking subsidiaries in more than one state. One of these organizations controlled banking subsidiaries in 11 states, one had banking subsidiaries in seven states, two had subs in five states, four had banking subsidiaries in three states and the remainder were represented in only two states (Table 1). In total these 21 banking organizations control 138 banks and 1,369 branch offices in 22 states. This means that almost half of our states house banks controlled by out-of-state holding companies.

In addition to domestic holding companies controlling interstate banks, seven international

10/4 22

Table 2. Foreign Banking Organizations Controlling Interstate Offices

State	Number of Foreign Banking Organizations Controlling Interstate Offices by State of Residence	Number and Type of Interstate Office Locations by Type of Office: Banks	Branches	Edge Acts	Agencies	Total Number of Interstate Offices Controlled by Foreign Banking Organizations Headquartered Outside the State
California	26	8	2	2	63	75
District of Columbia	—	—	1	—	—	1
Florida	1	—	—	6	22	28
Georgia	—	—	—	—	10	10
Hawaii	—	1	—	—	2	3
Illinois	1	1	36	3	—	40
Louisiana	—	—	—	—	1	1
Massachusetts	1	—	4	—	—	4
New York	58	3	37	2	18	60
Oregon	—	—	7	—	—	7
Pennsylvania	—	—	6	—	—	6
Texas	—	—	—	9	—	9
Washington	—	—	10	—	—	10
	103*	13	103	22	116	254

*16 of these organizations that have offices in more than one state are international organizations having no resident state—i.e. agency offices of international banks.

Source: Federal Reserve Bank of New York, as of 6-30-82.

banking organizations control banks in more than a single state. Table 1 identifies and locates these organizations. Prior to the Bank Holding Company Act of 1956, international organizations could establish banks in more than one state. Following 1956, however, any international organization controlling more than one U.S. bank fell under the Holding Company Act and became subject to the Douglas Amendment. Grandfather provisions allowed these organizations to continue their interstate system but restricted the organization from expanding outside its declared home state. In total, seven international bank holding companies control seven banks in states other than the state in which they are based. Of the seven foreign holding companies controlling banks in more than one state, five declared New York as their state of residence and two declared California (Table 2).

Fifty-three international banks have interstate branches, 25 of which are home officed in New York and 24 in California. As Table 2 shows, 71 percent of their interstate branches (73 in number) are located in either New York or Illinois. As would be expected, most of the interstate branches of foreign banks are located in our larger cities and trade centers. These organizations then have established an interstate presence of full service banks in some of our most attractive markets.

In addition to the 103 interstate branches established by foreign banks, they have established 116 interstate agency offices and 22 interstate Edge Act offices. This brings the total number of interstate offices of foreign banks and holding companies to 254 (Table 2).

The door to interstate banking is not completely closed. The Douglas Amendment allows bank holding companies to acquire banks on an interstate basis if the target state passes legislation that specifically allows out-of-state holding companies to acquire instate banks. To date, five states have passed such legislation.[1] Two other

[1] Utah passed reciprocal legislation in 1981 but repealed same in 1983.

1014AAA

Table 3. Interstate Savings and Loan Associations and Their Geographic Coverage
(March 7, 1983)

Parent	Home Office Locations	Interstate Locations
1. Northeast Savings, F.A.	CT	CT, MA, NY
2. City FS & LN	NJ	NJ, FL
3. Empire of America, FSA	MI	MI, FL, NY, TX
4. Carteret S&LA, FA	NJ	NJ, FL
5. Perpetual American FS&LA	VA	VA, DC, MD
6. Home Savings of America, FS & Los Angeles	CA	CA, FL, IL MO, TX
7. Glendale FS&LA	CA	CA, FL
8. First Nationwide Savings FS & LA	CA	CA, NY, FL
9. California FS & LA	CA	CA, GA, FL, NV
10. World S&LA, A FS&LA	CA	CA, KS, CO
11. First FS&LA of Arizona	AZ	AZ, TX
12. Bay Savings Bank	MI	MI, VA
13. National Permanent FS&LA	DC	DC, MD
14. First FS&LA of Puerto Rico	PR	PR, VI
15. Charter FS&LA	GA	GA, AL
16. Equitable FS&LA	MD	MD, DC
17. Union FS&LA of Evansville	IN	IN, KY
18. Farm and Home SA	MO	MO, TX
19. Mountainwest S&L	UT	UT, WY
20. The Benj Franklin FS&LA	OR	OR, ID, WA, UT

Source: Federal Home Loan Bank Board

states, Delaware and South Dakota, allow entry through limited purpose banks, and both have actually experienced entry by out-of-state holding companies. In addition, Iowa, Illinois, and Florida allow expansion by out-of-state banking organizations that operate banks or trust companies under grandfather provisions.

Although interstate deposit-taking is prohibited, many interstate banking services exist, and more could develop in the future even without changes in the federal laws prohibiting interstate banking. Three recent avenues for establishing an interstate banking presence or position are through the purchase of up to 5 percent of voting stock, preferred convertible stock,and franchise agreements among banks.

The Bank Holding Company Act specifies that it "shall be unlawful, except with the prior approval of the Board, ... for any bank holding company to acquire directly or indirectly ownership or control of any voting shares of any bank, if after such acquisition, such company will directly or indirectly own or control more than 5 percent of the voting shares of such bank...."[2] This clause leaves the door open for bank holding companies to acquire up to 5 percent of the voting shares of a bank without Board approval. As a result, some bank holding companies have taken the opportunity to invest in banks across state lines, establishing associations of banks that may work together for their common benefit. These investments have taken the form of 4.9 percent voting stock ownership, nonvoting preferred stock that automatically converts to voting stock should the prohibition on interstate banking be removed, or simple franchise agreement among banks.

Whatever the path, the result is a potential interstate network of banks large enough and geographically dispersed enough to offer products and services no one bank may have been capable of offering separately. These formal and informal agreements represent a form of geographic

[2]Section 3(a) Bank Holding Company Act of 1956.

1014 BBB

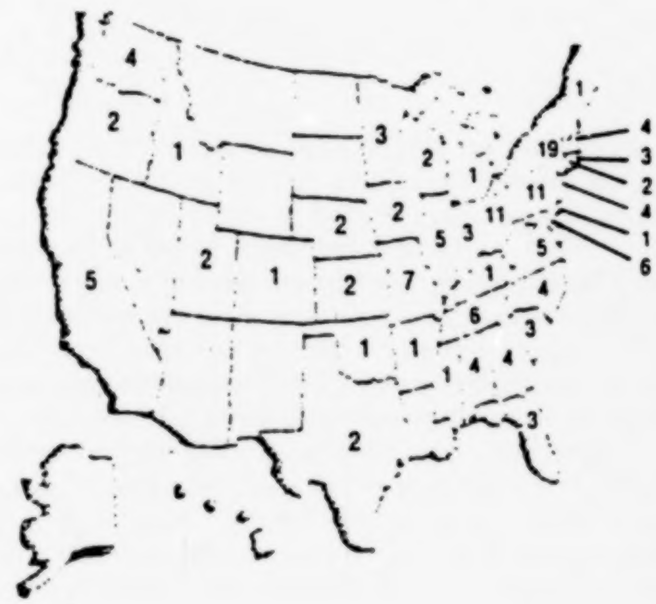
positioning for the day when interstate powers are granted. Texas Commerce Bankshares, for example, has investments in banks in Wyoming, Colorado, Arizona, Oklahoma and Louisiana.[3] While no comprehensive list of these investments and agreements was available, we are aware of these methods to establish an interstate presence. To date the Federal Reserve Board has approved two preferred stock deals, has disapproved one which is being restructured and has at least seven others pending.

The Bank Holding Company Act does not prohibit individuals from acquiring more than one bank. Neither does it require individuals to file an application with the Board regarding the acquisition of bank stock either within a given state or on an interstate basis.[4] We know that interstate banking groups controlled by individuals exist, but we have no accurate measure of the number of these groups or the number and geographic dispersion of the banks involved. To this extent, our inventory again is understated.

Another avenue for interstate expansion was opened by the emergency provisions of the Depository Institutions Act of 1982 allowing out-of-state organizations to acquire troubled banks and insured mutual savings banks under certain circumstances.[5] Although these provisions have not been used to allow interstate bank acquisitions to date, they do provide an avenue for interstate expansion.[6] The Federal Home Loan Bank Board began allowing interstate mergers of savings and loans in 1981, allowing only four that year. In 1982, however, 16 such mergers were allowed and today 29 interstate savings and loan systems exist (Table 3). Although these cases are limited, the provisions of the Garn-St Germain Depository Institutions Act and the fact that the Federal Home Loan Bank Board is actively allowing S&Ls to merge across state lines indicates increasing pressure for further relaxation of the prohibition on interstate banking.

Commercial banks are the only financial services suppliers effectively constrained geographically today, and even these constraints do

Map 1
Resident State of Bank Holding Companies Controlling Interstate 4(c)8 Subsidiaries



Total: 139

not apply to all commercial banks under all conditions. The fact that a commercial banking organization in one state may acquire a failing institution in another state inevitably will result in commercial banks facing competition from interstate banking organizations.[7] Because of the criteria for such acquisitions, the degree of competition may be limited at first; yet as the failing institution recovers and takes advantage of its association with an interstate parent, local bank competitors will resent such relationships. Geographically constrained banking organizations will feel that a two way competitive street is necessary. As the number of such acquisitions across state lines increases, support for repeal of interstate bank prohibitions will also increase. The emergency provisions of the Depository

[3] United States Banker, January 1983, p. 15.
[4] See "Change in Bank Control Act," Title VI of the Financial Institutions Regulatory and Interest Rate Control Act of 1978.
[5] See footnote 1.
[6] The Depository Institution Act of 1982 allows closed insured commercial banks with assets of $500 million or more and insured mutual savings banks with assets of $500 million or more and in danger of failing to be acquired by an out-of-state bank or bank holding company with priority given in the following order: acquisition of similar institutions in the same state; acquisition by same type of institution in different states; acquisition by different types of institutions in the same state; and acquisition by different types of institutions in different states.
[7] The degree of interstate expansion through the emergency provisions will be limited by the requirement that the failing institution must have at least $500 million in assets. It may be possible, however, for a number of weak institutions to be consolidated in order to meet this requirement. An organization in Tennessee is currently attempting such a consolidation.
[8] Section 2(c) of the Bank Holding Company Act of 1956.

1014 CCC

Institutions Act of 1982 may in fact be unlocking the door to full interstate banking.

Given the number of interstate banking organizations, the extent of their geographic coverage, the other unmeasured forms of interstate banking, and the potential avenues for still further expansion, the actual extent of interstate banking is probably far greater than might be assumed given the laws prohibiting it.

Nonbank Subsidiaries

For purposes of the Bank Holding Company Act, a bank is defined as "... any institution ... which (1) accepts deposits that the depositor has a legal right to withdraw on demand, and (2) engages in the business of making commercial loans."[8] Therefore an organization that offers both demand deposits and commercial loans may be defined as a commercial bank, and, hence, would fall under the interstate banking restrictions. The laws prohibiting interstate banking limit the ability of a formal banking organization to offer both demand deposits and commercial loans at a single location in more than one state. But by separating the demand deposit and commercial lending functions it is possible for banking organizations to circumvent the interstate restrictions and provide interstate financial services. Indeed, nothing prevents a commercial bank in one state from advertising and accepting demand deposits or savings deposits from consumers in another state. Many large commercial banks aggressively sell large certificate of deposits on an interstate basis. They employ calling officers to seek out major accounts nationwide, and they market their credit cards nationwide. In addition, commercial banks are offering such financial services as cash management, electronic funds transfer accounts, loan participations and a variety of correspondent banking services that know no state boundary. These are all examples of services offered across state lines that do not require the bank to establish a physical presence.

By separating the demand deposits and commercial lending functions, however, a banking organization can establish a physical presence across state lines. One way for bank holding companies to accomplish this is through the creation or acquisition of nonbank subsidiaries. The nonbank subsidiaries do not constitute a commercial bank and, hence, are free to open offices on an interstate basis. National banks may undertake a number of the same 4(c)8 type activities allowed to bank holding companies (Table 4). For the most part, however, these activities are constrained to the state in which the parent bank is located.

Identifying Interstate 4(c)8 Offices

With the assistance of the eleven other Federal Reserve District Banks, we were able to piece together a composite picture of holding companies throughout the nation that controlled interstate 4(c)8 subsidiaries and the number of interstate offices each controlled. Although an application is required prior to a 4(c)8 subsidiary opening a new office, no consolidated records were available. Each District Federal Reserve Bank compiled a list of holding companies with interstate 4(c)8 offices and provided the office locations on a state-by-state basis. In a few instances it was necessary to contact holding companies directly to obtain the desired information. This article presents the best information available on 4(c)8 interstate activity, but the data may not be 100 percent inclusive. The numbers represent an actual count of those institutions and office locations of those institutions we identified as being involved in 4(c)8 services on an interstate basis. Therefore, the numbers may understate the extent of interstate activity.

In total there are 3,201 one-bank holding companies and 430 multibank holding companies in the United States (Table 5). Of the 3,631 holding companies capable of establishing or acquiring interstate offices of 4(c)8 subsidiaries, only 139 or approximately four percent elected to do so. Of those 139, 68 were one-bank and 71 were multibank holding companies. One common characteristic of holding companies electing to go interstate through their 4(c)8 subsidiares was their absolute size. Of the 50 largest banking organizations in the country, 42 have interstate 4(c)8 subsidiaries. Of the 100 largest banking organizations, 70 have 4(c)8 subsidiaries that control interstate offices; of the top 150 organizations, 102 have interstate 4(c)8 subsidiaries. Therefore, as a generalization, large bank holding companies are the most likely to provide interstate financial services through offices of their 4(c)8 subsidiaries. They are also the organizations most likely to undertake interstate banking if or when the prohibitions are lifted.

Table 5 also indicates that these 139 holding companies control 382 4(c)8 subsidiaries which collectively have at least 5,500 offices outside

1014 DDD

Allowable Nonbank Activities

The Bank Holding Company Act of 1956 as amended in 1970 defines a bank holding company as"—any company which has control over any bank or over any company that is or becomes a bank holding company by virtue of this Act." The term company includes all legal entities except individuals—that is, corporations, partnerships, trusts or associations. Individuals are excluded and consequently may own any number of banks or other financial institutions in any number of states without coming under the provisions of the act. For purposes of the act, the term "control" was defined as controlling directly or indirectly 25 percent or more of any class of voting securities of the bank or company, or controlling the election of a majority of directors or trustees of the bank or company, or the Board of Governors of the Federal Reserve System determines that the company directly or indirectly exercises a controlling influence over the management or policies of the bank or company.[9] This latter provision gives the Board of Governors wide latitude in determining what constitutes control, and hence, what is or is not a holding company.

Section 4(c)8 of the Bank Holding Company Act states the criteria the Board must apply before allowing bank holding companies to engage in certain nonbank activities. Some of those nonbank activities are prohibited to individual banks, but the majority are activities in which nationally chartered banks may engage.[10] Under 4(c)8, a bank holding company may be exempted from the general prohibition against acquiring or establishing nonbank activities and allowed to acquire.

> "shares of any company the activity of which the Board after due notice and opportunity for hearing has determined (by order or regulation) **to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.** In determining whether a particular activity is a proper incident to banking or managing or controlling banks the Board shall consider whether its performance by an affiliate of a holding company can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest, or unsound banking practices."

To be considered a permissible nonbank activity for bank holding companies, the activity must pass two tests. First, it must be closely related to the activities in which banks engage. This is a rather vague criterion in light of the "incidental powers" accorded banks through Section 8 of the National Bank Act of 1864 which states that banks may "exercise... all such incidental powers as shall be necessary to carry on the business of banking...". Given this vagueness it is not surprising that the Board of Governors has no published statement of the criteria it uses to determine activities closely related to banking. Researchers have observed, however that the Board has approved activities in which banks have historically engaged, or activities complementing services normally provided by banks or activities in which banks clearly possess technical skills.[11] If the activity satisfies at least one of these criteria, it may be proclaimed a permissible activity if it also passes the second test: that providing the service through a nonbank subsidiary may reasonably be expected to produce net public benefits.

The Board may approve a nonbank activity either by order or by regulation—adding the activity to the "laundry list" of approved activites as set forth in Regulation Y, Section 4(c)8. If the activity is approved by order, then every future applicant wishing to undertake that activitiy must justify the activity to the Board. Effectively, this amounts to a case-by-case review and opinion. On the other hand, if the activity is approved and added to approved activities listed in the regulation, a future applicant need not justify the activity and an application may be approved under delegated authority at the Reserve Bank level if all other conditions for delegated authority are met.

To date, the Board has approved and added to the "laundry list" 17 activities in which bank holding companies may engage by either establishing *de novo* nonbank subsidiaries or acquiring nonbank subsidiaries. The approved activities are set forth in Table 4.

Through an application process, one bank and multibank holding companies may gain approval to establish a nonbank subsidiary to engage in any or a combination of activities. By definition, a nonbank subsidiary is not a bank and, hence, does not fall under regulations or laws that apply only to banks. The nonbank entities are, therefore, capable of unrestricted geographic expansion both intrastate and interstate.[12] Since the vast majority of the approved nonbank activities are activities in which banks may engage, i.e. "activities which are closely related to banking or managing or controlling banks...",the 4(c)8 provisions effectively allow bank holding companies to provide financial services similar to those provided by banks but on an interstate basis.

---

[9] See Statutory Appendix to Regulation Y.

[10] See Dale S. Drum, "Nonbanking Activities of Bank H[illegible] Companies Economic Perspective, Federal Reserve Bank of Chi[illegible] March/April, 1977.

[11] See for example, Harvey Rosenblum, "Bank Holding Companies: An Overview" Business Conditions, Federal Reserve Bank of Chicago, August, 1973; or Samuel H. Talley: "Developments in the Bank Holding Company Movement", Proceedings of a Conference on Bank Structure and Competition, 1972, Federal Reserve Bank of Chicago.

[12] In two cases, bank holding companies have received approval to acquire troubled S&Ls with the condition that bank branching laws would apply to the acquired S&Ls.

1014 333

Table 4. Permissible Nonbank Activities for Bank Holding Companies Under Section 4(c)8 of Regulation Y
February, 1983

Activities permitted by regulation

1. Extensions of credit[2]
   Mortgage banking
   Finance companies: consumer, sales, and commercial
   Credit cards
   Factoring
2. Industrial bank, Morris Plan bank, industrial loan company
3. Servicing loans and other extensions of credit[2]
4. Trust company[2]
5. Investment or financial advising[2]
6. Full-payout leasing of personal or real property
7. Investments in community welfare projects[2]
8. Providing bookkeeping or data processing services[2]
9. Acting as insurance agent or broker primarily in connection with credit extensions[2]
10. Underwriting credit life, accident and health insurance
11. Providing courier services[2]
12. Management consulting for all depository institutions
13. Sale at retail of money orders with a face value of not more than $1000, travelers checks and savings bonds[1, 2]
14. Performing appraisals of real estate[1]
15. Issuance and sale of travelers checks[1]

Activities permitted by order

1. Issuance and sale of travelers checks[2, 6]
2. Buying and selling gold and silver bullion and silver coin[2, 4]
3. Issuing money orders and general-purpose variable denominated payment instruments[1, 2, 4]
4. Futures commission merchant to cover gold and silver bullion and coins[1, 2]
5. Underwriting cetain federal, state and municipal securities[1, 2]
6. Check verification[1, 2, 4]
7. Financial advice to consumers[1, 2]
8. Issuance of small denomination debt instruments[1]
9. Arranging for equity financing of real estate[1]
10. Acting as futures commissions merchant[1]
11. Discount brokerage[1]
12. Operating a distressed savings and loan association[1]
13. Operating an Article XII Investment Co.[1]
14. Executing foreign banking unsolicited purchases and sales of securities
15. Engaging in commercial banking activities abroad through a limited purpose Delaware bank[1]
16. Performing appraisal of real estate and real estate advisor and real estate brokerage on nonresidential properties[1]
17. Operating a Pool Reserve Plan for loss reserves of banks for loans to small businesses[1]
18. Operating a thrift institution in Rhode Island
19. Operating a guarantee savings bank in New Hampshire[1]
20. Offering informational advice and transactional services for foreign[1] exchange services

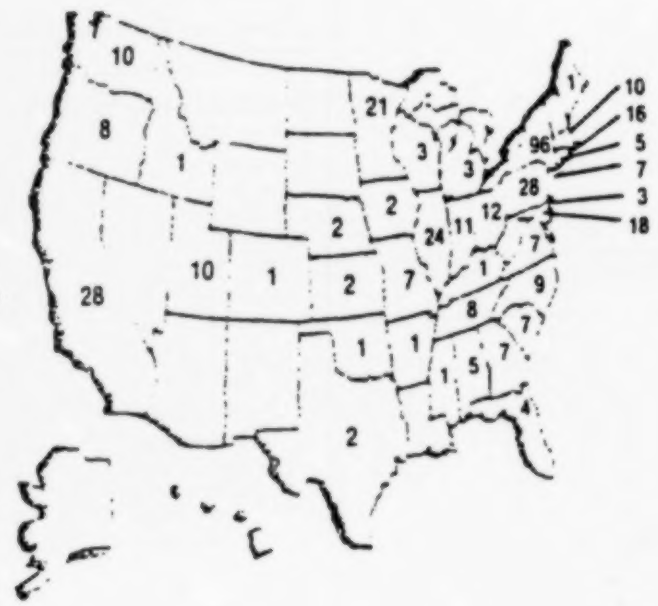
Activities denied by the Board

1. Insurance premium funding (combined sales of mutual funds and insurance)
2. Underwriting life insurance not related to credit extension
3. Sale of level-term credit life
4. Real estate brokerage (residential)
5. Armored car
6. Land development
7. Real estate syndication
8. General management consulting
9. Property management
10. Computer output microfilm services
11. Underwriting mortgage guaranty insurance[3]
12. Operating a savings and loan association[1, 5]
13. Operating a travel agency[1, 2]
14. Underwriting property and casualty insurance[1]
15. Underwriting home loan life mortgage insurance[1]
16. Investment note issue with transactional characteristics[1]
17. Real estate advisory services[1]

[1]Added to list since January 1, 1975.
[2]Activities permissible to national banks.
[3]Board orders found these activities closely related to banking but denied proposed acquisitions as part of its "go slow" policy.
[4]To be decided on a case-by-case basis.
[5]Operating a thrift institution has been permitted by order in Rhode Island, Ohio, New Hampshire and California.
[6]Subsequently permitted by regulation.
Source: Federal Reserve Board

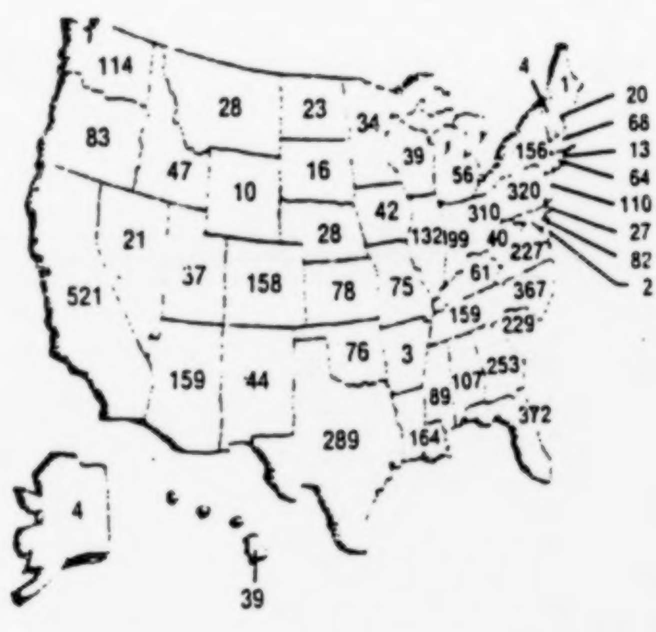
1014 FFF

Map 2
Number of Interstate Subsidiaries of Holding Companies Home Officed in the State



Total: 382

Map 3
Total Number of Offices: All 4(c)8 Subsidiaries



Total: 5,500

the state in which the parent holding company resides. Map 1 indicates that 56 of these holding companies (41 percent of the total) with interstate 4(c)8 subsidiaries reside in 10 northeastern states (Maine, New York, Massachusetts, Rhode Island, Connecticut, Pennsylvania, New Jersey, Delaware, Maryland and Virginia). The highest concentration of holding companies controlling 4(c)8 subsidiaries with interstate offices is in the northeastern portion of the nation.

Map 2 shows the number of 4(c)8 subsidiaries controlled by holding companies home officed in a given state. In total the 139 holding companies control 382 4(c)8 subsidiaries with interstate offices. Approximately fifty percent of the 4(c)8 subsidiaries (191) have parent holding companies that reside in the Northeast, specifically the northeastern coastal states from Virginia to Maine plus Pennsylvania (Maine, New York, Massachusetts, Rhode Island, Connecticut, Pennsylvania, New Jersey, Delaware, Maryland and Virginia). And as Map 3 shows, these 191 subsidiaries controlled better than 64 percent (3,472) of all interstate 4(c)8 offices. Therefore, the vast majority of holding companies controlling 4(c)8 subsidiaries with interstate offices are based in the Northeast. In fact, New York and Pennsylvania alone accounted for 22 percent (30) of all holding companies with interstate 4(c)8 subsidiaries. Holding companies in those two states controlled 124 separate interstate subsidiaries, 33 percent of the total, and 1,874 (34 percent) of the total interstate offices. This is not surprising given the number of large holding companies in this area. If interstate positioning through 4(c)8 subsidiaries is any indication, large organizations, especially those in the Northeast, are the most likely to become active in interstate banking if and when the laws permit.

Types of Financial Services Provided

A nonbank subsidiary may provide more than one 4(c)8 activity at a given location. For instance, a nonbank subsidiary primarily engaged in consumer finance activity may also provide credit life insurance and leasing activities. Therefore, there is a difference between the number of 4(c)8 services provided and the number of 4(c)8 subsidiaries and the number of offices of 4(c)8 subsidiaries. Table 6 summarizes the number of 4(c)8 activities provided through

1014 999

Table 5. Bank Holding Companies, Number with Interstate 4(c)8 Subsidiaries and Offices of Interstate 4(c)8 Subsidiaries by State

Home State of Holding Company	Total Number of Holding Companies Home Officed in State			Interstate Companies		
	One-Bank	Multi Bank	Total	Number of Holding Companies	Number of Subsidiaries	Number of Offices
Alabama	16	9	25	4	5	12
Alaska	3	1	4	—	—	—
Arizona	5	0	5	0	—	—
Arkansas	47	2	49	1	1	1
California	42	6	48	5	28	636
Colorado	104	22	126	1	1	1
Connecticut	7	3	10	2	5	13
D.C.	7	3	10	—	—	—
Delaware	12	1	13	1	3	1,171
Florida	48	29	77	3	4	50
Georgia	49	22	71	4	7	157
Hawaii	3	0	3	—	—	—
Idaho	6	1	7	1	1	2
Illinois	316	7	323	5	24	70
Indiana	66	1	67	3	11	38
Iowa	268	16	284	2	2	3
Kansas	323	8	331	2	2	2
Kentucky	43	1	44	1	1	5
Louisiana	47	1	48	—	—	—
Maine	2	4	6	1	1	1
Maryland	3	4	7	6	18	102
Massachusetts	14	13	27	4	10	34
Michigan	18	24	42	1	3	6
Minnesota	286	15	301	3	21	585
Mississippi	26	0	26	1	1	2
Missouri	175	40	215	7	7	7
Montana	34	7	41	—	—	—
Nebraska	283	0	283	2	2	2
Nevada	2	0	2	—	—	—
New Hampshire	6	4	10	—	—	—
New Jersey	8	11	19	4	7	17
New Mexico	19	4	23	—	—	—
New York	19	11	30	19	96	1,593
North Carolina	9	1	10	4	9	226
North Dakota	51	4	55	—	—	—
Oklahoma	250	6	256	1	1	1
Ohio	16	17	33	11	12	12
Oregon	3	5	8	2	8	27
Pennsylvania	32	3	35	11	28	283
Rhode Island	11	0	11	3	16	167
South Carolina	5	0	5	3	7	86
South Dakota	41	4	45	—	—	—
Tennessee	40	10	50	6	8	14
Texas	283	59	342	2	2	2
Utah	17	5	22	2	10	37
Vermont	4	1	5	—	—	—
Virginia	5	9	14	5	7	86
Washington	7	1	8	4	10	42
West Virgina	9	1	10	—	—	—
Wisconsin	82	28	110	2	3	7
Wyoming	29	6	35	—	—	—
TOTAL	3,201	430	3,631	139	382	5,500

Source: Federal Reserve Board Data Base as of December 31, 1981.

Note: Data on holding companies with interstate subsidiaries is based on data from the District Federal Reserve Banks except in the 11th and 12th Federal Reserve Districts where we contacted the holding companies. This data based on December 31, 1981, figures, is a snapshot of a constantly changing situation and is not intended as an exhaustive listing.

1014 HHH

interstate offices of nonbank subsidiaries by section of the country. At least 4,613 offices of nonbank subsidiaries of out-of-state bank holding companies provide consumer finance services, by far the most popular type of interstate 4(c)8 activity for bank holding companies to engage in. The second most popular is the insurance agency activity (provided through 2,440 offices), followed by underwriting credit life (1,118 offices), servicing loans (1,995 offices), mortgage banking (623 offices) and leasing (580 offices).[13] Interstate offices that provide check verification, audit services, and credit cards are the least popular. Although these services are provided on an interstate basis, they don't require permanent physical presence.

The geographic distribution of these services is interesting. The South Atlantic (Census Region) states lead the nation in the number of activities provided through nonbank subsidiaries belonging to out-of-state holding companies. These South Atlantic states house 1,327 offices of out-of-state holding companies providing consumer finance services, 214 offices offering mortgage banking and 21 offices offering trust services. The Pacific states are the second most popular target for most 4(c)8 activities, but these states house less than half the number of activities provided through offices in the South Atlantic region. Quite obviously, a region's size plays a part in these statistics, but generally the primary targets for 4(c)8 activities appear to be the faster growing states with substantial populations. In terms of total number of activities offered through nonbank subsidiaries of out-of-state holding companies, California leads the way with 907, followed by Florida with 824, North Carolina with 769, Pennsylvania with 640, Ohio with 614, South Carolina with 558, Georgia with 557 and Texas with 542. The remaining 42 states house approximately the same number of activities offered through offices of nonbank subsidiaries of out-of-state holding companies as the total offered in these 8 states.

Interstate Offices by Primary Activity

As noted above, more than one 4(c)8 activity may be provided through a single subsidiary office. Many activities are low profile and normally provide a complementary service to some other 4(c)8 activity. For example, as Table 6 indicates, the insurance agent activity is provided at 2,440 locations, although the interstate offices of 4(c)8 subsidiaries primarily engaged in this activity number only 40. The same is true for underwriting credit life insurance; while credit life insurance is provided at 1,118 offices of 4(c)8 subsidiaries, only 56 are primarily engaged in this activity. Therefore, to assess the geographic extent to which bank holding companies are establishing a physical presence on an interstate basis, one should focus on the number of 4(c)8 offices by primary activity. A table detailing the number of these offices by primary activity and by region is available from the Atlanta Fed.

At least 5,500 offices of 4(c)8 subsidiaries are located outside the state in which the parent company resides. Four of the primary activities are what may be considered high profile activities: finance company, mortgage banking, industrial banking and trust services. While offices of some of the other primary activities establish the holding company's presence in an area, they are less visible to the public. In addition, these four highly visible activites accounted for 5,189 of the interstate 4(c)8 offices, or 95 percent of the total. Finance companies dominate as the most popular type of primary 4(c)8 activity. In total, subsidiaries of bank holding companies control 4,442 finance company offices outside the state in which the parent company resides. This one activity accounts for better than 80 percent of all interstate 4(c)8 offices.

A look at the geographic distribution of interstate offices of 4(c)8 subsidiaries may indicate which states or areas of the country will be the primary targets for interstate expansion if the prohibition on interstate banking is lifted. Map 3 shows by state the number of 4(c)8 offices controlled by out-of-state holding companies. In terms of total office locations, California has attracted more activity than any other state with 521 offices. Florida is a distant second with 372 offices, closely followed by North Carolina (367), Pennsylvania (320), Ohio (310) and Texas (289).[14] Five southeastern Atlantic coast states have attracted a good deal of the attention of out-of-state holding companies—Virginia, North

[13] Any location at which a customer may obtain credit life insurance which is reinsured by a holding company subsidiary is included in the 1,118 offices providing underwriting credit life.

[14] Pennsylvania has very attractive usury laws which may explain at least in part the degree of nonbank entry.

1014 III

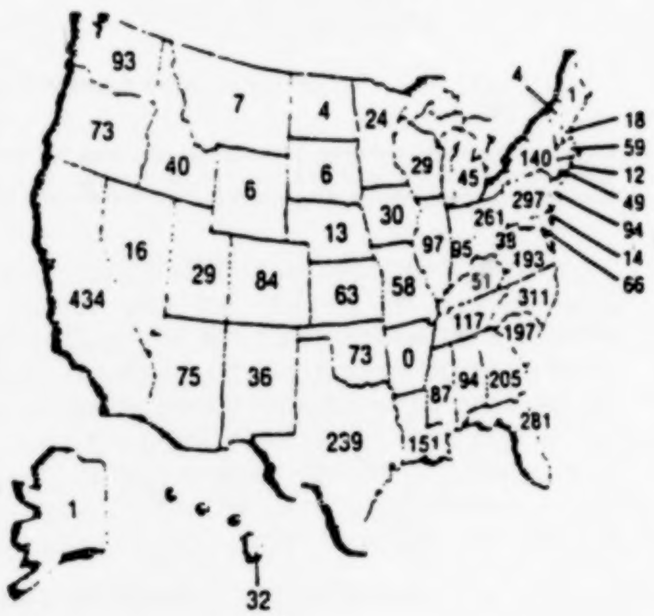
Table 6. Interstate Nonbank Subsidiaries: Location of Activities by Region

TYPE OF ACTIVITY	New England	Mid Atlantic	South Atlantic	W. South Central	E South Central	North Central-East	North Central-West	Pacific	Mountain	TOTAL
Mortgage Banking	19	27	214	47	61	74	32	80	69	623
Finance Company	149	536	1,327	466	389	565	208	652	321	4,613
Credit Cards	0	0	5	0	0	0	1	0	0	6
Factoring	1	5	10	9	3	3	1	12	4	48
Industrial Bank	2	0	29	1	1	2	18	23	49	125
Servicing Loans	47	140	334	83	32	105	45	106	103	995
Trust Company	0	4	21	0	2	1	13	7	20	68
Financial Advisor	2	2	29	17	1	17	1	12	11	92
Leasing	30	86	167	53	14	114	23	49	44	580
Investment in Community Welfare	0	0	0	0	0	4	0	4	4	12
Data Processing	2	3	6	4	1	9	16	3	10	54
Insurance Agent	72	230	836	253	236	251	97	273	192	2,440
Underwriting Credit Life	21	45	407	106	83	78	65	159	154	1,118
Management Consulting	0	0	2	3	0	0	1	2	2	10
Money Orders, Travelers Checks	0	0	113	2	42	12	0	4	4	177
Check Verification	0	0	2	0	1	0	0	0	0	3
Audit Services	0	0	0	0	0	0	4	0	1	5
Total Per Region	345	1,078	3,502	1,044	866	1,235	525	1,386	988	
Total for U.S.										10,969

Source: Federal Reserve Bank of Atlanta

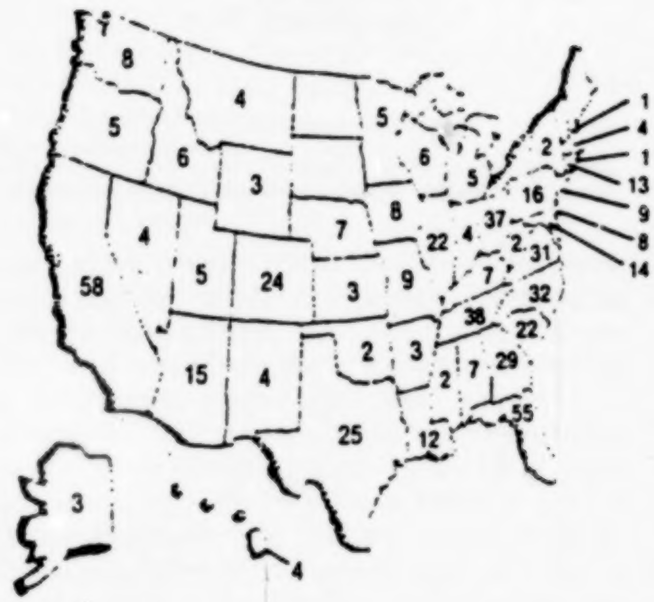
1014 JJJ

Map 4
By Major 4(c)8 Activity and Number of Offices Located in each State
Finance Companies



Total: 4,442

Map 5
By Major 4(c)8 Activity and Number of Offices Located in each State
Mortgage Banking



Total: 584

Carolina, South Carolina, Georgia and Florida. Combined, these states constitute a land mass half again as large as California but house almost three times the number of 4(c)8 offices, 1,447 offices of out-of-state holding companies (27 percent of the total). Indeed, these five states and Pennsylvania, Ohio, Texas and California have been the most attractive for interstate expansion through 4(c)8 subsidiaries and, if we may use this as any indication, will probably be the most attractive targets for interstate bank expansion should the prohibition be removed.

Map 4, again, reveals that most interstate 4(c)8 activity has been consumer finance oriented. Over 83 percent of all interstate 4(c)8 offices in the nine states mentioned above as attractive targets were finance companies. In fact, 93 percent of all 4(c)8 offices in Pennsylvania are finance companies. This may be interpreted as evidence that these states would be especially attractive for consumer-oriented banks.

Map 5 shows a more or less consistent pattern for mortgage banking offices with the exception that Tennessee and Illinois should be added to our list of attractive states.

Footnote 15 lists the number of office locations of all 4(c)8 subsidiaries engaged primarily in offering trust services.[15] Florida is obviously the prime target for such activities—again a consumer or retail-oriented service. Part of this pattern, however, may be due to the relative leniency of restrictions that states place on entry via the trust route. Florida, for example has no restrictions on out-of-state organizations establishing trust companies in the state.

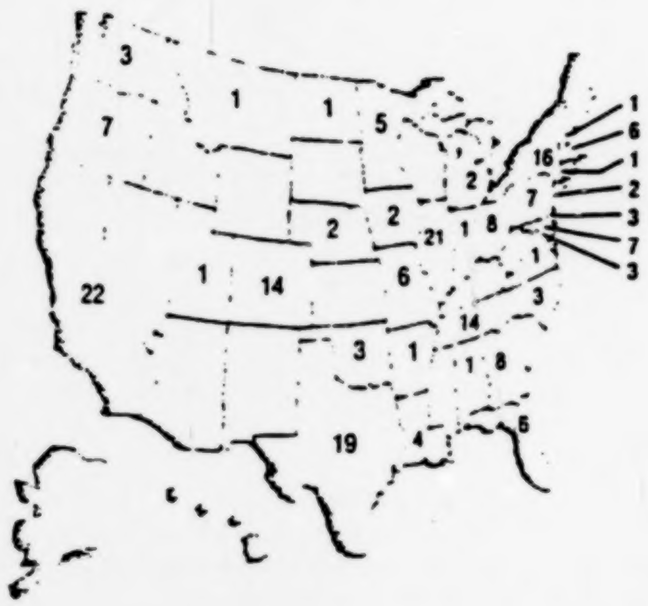
State laws restricting industrial banks also play a part in the geographic distribution of this 4(c)8 activity.[16] Although there is some activity in the Carolinas and Georgia, many states prohibit such organizations. A number of midwestern and western states do allow industrial banks, and that is where most such offices are located.

[15] Trust companies (number of offices in each state) - Florida (20), Arizona (9), Montana (8), North Dakota (3), South Dakota (4), New York (3), Nebraska (2), Pennsylvania (1), Hawaii (1), California (1), Illinois (1), and Tennessee (1).

[16] Industrial Banks (number of offices in each state) - Colorado (40), North Carolina (12), Kansas (12), California (10), Georgia (9), South Carolina (7), Washington (8), Utah (20), Hawaii (2), Arizona (10), Nebraska (1), and Florida (1).

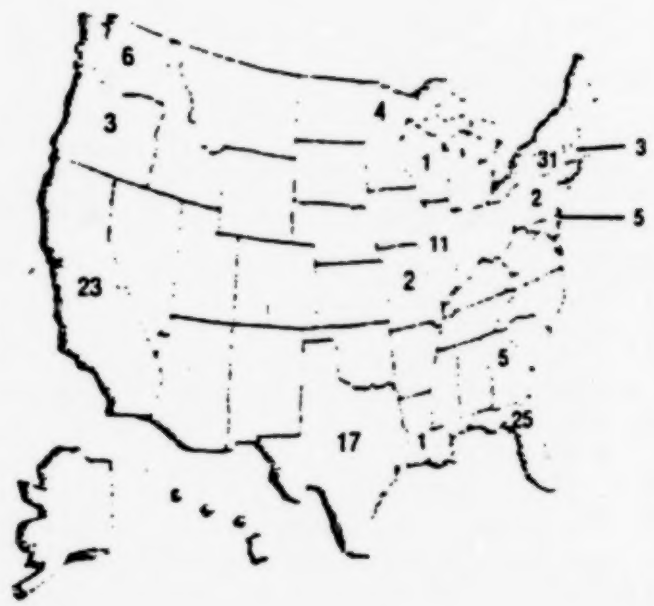
1014 KKK

Map 6
Interstate Loan Production Offices
Located in each State



Total: 202

Map 7
Interstate Edge Act Office Domestic Banking
Organization



Source: Federal Reserve Bank of New York
(As of Oct. 1982)

Total: 143

To the extent that offices primarily engaged in the leasing activity may be used to indicate the wholesale banking function, it appears that California, Texas and Ohio will be prime targets for wholesale banking should the laws permit. Each of these states houses at least 10 offices of out-of-state bank holding companies' 4(c)8 subsidiaries. North Carolina, Illinois Missouri and Florida also would appear to be desirable targets from this perspective.[17]

Other Nonbank Subsidiaries

In addition to 4(c)8 subsidiaries, banking organizations are permitted to establish loan production offices and Edge Act corporations on an interstate basis. Loan production offices can do little more than a calling officer, but they are useful in establishing a wholesale presence in an area. Edge Act offices are also aimed at wholesale customers but are limited to dealing with organizations engaged in international trade.

Since regulatory agencies do not track data on loan production offices, it was necessary to survey banking organizations directly. Only the largest banking organizations are likely to commit resources to loan production offices, especially in light of the fact that calling officers may provide the same services without a physical presence in an area. Therefore we surveyed the top 200 banking organizations in the country and found that they controlled a total of 202 loan production offices.

Table 7 shows the number of banking organizations in each state that have established out-of-state loan production offices, the number of offices established and the number of states in which these offices have been placed. Map 6 shows that California, Illinois, Texas, New York, Colorado and Tennessee have attracted more loan production offices than other states.

Following the same logic, Edge Act corporations are established in order to follow the geographic distribution of one's customers engaged in international trade. There are 143 interstate

[17]Leasing activities (number of offices in each state) - Texas (11), California (10), Ohio (10), Illinois (8), North Carolina (8), New Jersey (5), Missouri (5), Florida (5), New York (4), Colorado, Michigan, Kentucky, Tennessee, Pennsylvania (3 each), Delaware, Washington, Minnesota (2 each), Montana, Arizona, New Mexico, Nebraska, Louisiana, Georgia, South Carolina, Connecticut (1 each).

1014 LLL

Table 7. Interstate Loan Production Offices

Parent State	Number of Organizations Establishing Loan Production Offices	Number of Interstate Loan Production Offices Maintained	Number of States Entered by LPO's
California	5	36[a]	14
District of Columbia	1	7	7
Florida	1	1	1
Illinois	4	31	13
Kentucky	2	8	7
Maryland	1	3	3
Massachusetts	3	14	12
Michigan	1	1	1
Minnesota	2	5	5
Missouri	2	22[b]	6
New Jersey	1	2	2
New York	8	31[c]	13
North Carolina	2	4	2
Oklahoma	1	1	1
Pennsylvania	2	4	2
Rhode Island	2	6	5
Texas	2	5	3
Virginia	2	12	5
Washington	2	9	7
TOTAL	44	202	34

Notes:
[a] Only 3 LPOs from California are in New York
[b] General Bancshares Corporation of St. Louis, MO has full service banks in Missouri, Illinois, and Tennessee. They have 13 LPOs in Tennessee and 4 LPOs in Illinois.
[c] 10 of the 31 are in California

Source: FRB—Atlanta Survey of Largest 200 Banking Organizations; data as of December 31, 1982.

Edge Act offices of domestic organizations located in the United States. Map 7 shows their geographic distribution. Predictably, states with international trade centers have attracted the most Edge Act offices. New York attracted the largest number, 31, closely followed by Florida with 25 offices. California follows with 23, Texas with 17 and Illinois is a distant fifth with 11 Edge Act offices. New York, Florida, California and Texas are prime targets for this type of wholesale banking. Since only the largest banks may offer services needed by international corporations, banking organizations in the money centers have already located offices to serve these needs. For example, New York banks have established 15 Edge Act offices in California and California organizations have established five such offices in New York. Interstate banking would allow these organizations to provide little more wholesale services than they are providing today.

Summary of Interstate Activity

Table 8 summarizes by state the number of interstate offices of out-of-state banking organizations. The most impressive aspect is the fact that domestic banking organizations control at least 7,383 interstate offices and, if we include interstate offices of foreign banking organizations, the total reaches 7,840. This compares to a total of 55,440 banking offices in the nation. Almost 1,500 of the identified interstate offices supply all banking services. The remaining offices are nonbank subsidiaries offering a more limited number of banking type services. The sheer number of interstate offices controlled by holding companies is impressive, given the prohibition on interstate banking.

Holding companies may use a number of avenues to serve both interstate retail and wholesale customers. The only area in which they cannot effectively compete for consumer accounts is in the convenience area—providing

1014 MMM

171A

Table 8. Summary of Interstate Activity

LOCATION	GRANDFATHERED DOMESTIC Holding* Companies	Banks	Branches	GRANDFATHERED FOREIGN* Holding* Companies	Banks	Branches	FOREIGN BANKS Agency	Edge	Branch	States* With Reciprocal Agreement	Preferred* Stock Deals Filed With Board	Interstate* S&Ls	Offices of 4(c) 8 Subs	Loan Production Offices	Edge Act Corporations	Total Offices per State
Alabama											1	1	107	1		108
Alaska										✓			4	1		5
Arizona	1	1	161										159			321
Arkansas													3			3
California				8	8	148	63	2	2			2	521	22	23	787
Colorado	1	3	7									1	158	14		182
Connecticut											1		64	1		65
Delaware	12	12	40							O			27	3	8	87
District of Columbia									1			2	2	3		6
Florida	2	2	186				22	6		□	1	7	372	6	25	621
Georgia							10				1	2	253	8	5	278
Hawaii				1	1	16	2					2	39			57
Idaho	2	2	107									1	47			156
Illinois	1	3	4	1	1	1		3	36	□		1	132	21	11	212
Indiana													99	1		100
Iowa	1	11	50							□	1		42	2		105
Kansas												1	78			78
Kentucky												1	81			81
Louisiana							1						104	4	1	170
Maine										✓	1		1			1
Maryland	1	2	30									2	82	7		121
Massachusetts									4	✓	2	1	58	8	3	81
Michigan													56	2		58
Minnesota											1		34	5	4	43
Mississippi													89			89
Missouri												1	75	8	2	83
Montana	3	25	48									2	28	1		102
Nebraska	1	5	39										28	2		74
Nevada	1	1	66									1	21			88
New Hampshire													20	1		21
New Jersey													110	2		112
New Mexico	1	5	35										44			84
New York	1	7	27	3	3	39	18	2	37	✓	4	3	180	18	31	331
North Carolina													307	3		370
North Dakota	3	34	110										23	1		168
Ohio											2		310	8	4	322
Oklahoma											1		78	3		79
Oregon	1	1	169						7			4	83	7	3	270
Pennsylvania									8		2		320	7	2	335
Rhode Island													13			13
South Carolina											1		229			229
South Dakota	3	12	80							O			18			108
Tennessee	2	2	27										159	14		202
Texas								9			1	5	289	19	17	334
Utah	1	1	36							✓		1	37	1		74
Vermont													4			4
Virginia	1	6	83									1	227	1		297
Washington	1	1	86						10			2	114	3	8	219
West Virginia													40			40
Wisconsin	3	8	22										39		1	68
Wyoming	2	4	4									1	10			18
TOTALS	45	141	1,397	13	13	203	116	22	103	10	20	45	5,800	202	143	7,840

Notes

O - These states allow entry of limited purpose banks

□ - These states allow expansion of interstate grandfathered banks

* - These columns are not included in total number of offices

Δ - Six of the foreign bank holding companies own only one bank, but the bank is located outside the home state of the foreign banking organization.

1014 NNN

brick-and-mortar offices to attract small and medium sized consumer accounts.

On the wholesale side, holding companies are providing a wide array of interstate financial services, some of which require a physical presence but many of which do not. Many of these corporate services may be provided through nonbank subsidiaries, which are free to establish interstate offices. In addition, large banking organizations are providing large corporate customers with banking services not requiring physical interstate offices. These banking organizations appear to be competitively handicapped only in providing certain wholesale banking services to medium and especially small business customers. These customers still depend to a large extent on locally controlled banks.[18]

It appears, however, that as time goes by more and more of the financial services required by medium and small businesses will be targets for large banking organizations supplying these services through 4(c)8 provisions. It simply is not necessary for a banking organization to maintain a facility that both accepts deposits and makes loans to be competitive across state lines. The larger holding companies have already established their nonbank interstate presence.

Some of the smaller banking organizations having a regional scope are moving quickly to establish formal and informal agreements to form interstate networks if the interstate prohibitions are removed. Their rationale seems to be a perceived need to become large enough to compete with the money center banks on an equal footing. Although the smaller banking organizations make the assumption, the question is whether larger banking organizations are under any strong pressure to establish a nationwide interstate banking network involving brick-and-mortar offices. The answer must be a modified no.

First, the removal of Regulation Q means that banks will be required to pay money market rates for a larger proportion of their small and medium size deposits. The day of bank deposit customers subsidizing banks through low interest is over. Take this subsidy away and add in the expense of operating distant offices and one conclusion is clear: large banks have no great incentive to use brick and mortar facilities to collect deposits except possibly in the most attractive high growth markets.

From the consumer's standpoint the idea of interstate networks is also questionable. As banks are required to pay money market rates for more of their funds, they necessarily will have to pass the costs along to consumers through direct pricing on services. Since an interstate banking network will be expensive to maintain, will customers be willing to pay for the marginal benefits associated with "unlimited" geographic access to their accounts? The answer is probably "no," given the number of less costly alternatives available that do not require an interstate network. For these reasons it does not appear that the consumer will lead the way to interstate banking. Supply in this case will definitely follow demand—and little demand exists for this type of service.

Too many avenues allow banking organizations to provide interstate financial services on a less costly basis to believe that nationwide interstate brick-and-mortar expansion is inevitable.

Interstate bank expansion will occur in the absence of the interstate prohibition, but, because of the prodigious amount of interstate activity already in place, it will evolve slowly and will be geographically limited to the more attractive markets. There is some danger that small and medium sized banking organizations might be panicked into building interstate banking systems large enough to fend off money center banks. In the short run this may create some inefficient organizations. Taking a longer view, however, market forces will correct these inefficiencies. The larger money center banks, on the other hand, quite obviously will become active in the more attractive markets—but are unlikely to establish comprehensive nationwide interstate networks because they have already established themselves through nonbank subsidiaries.

—David D. Whitehead

[18] David Whitehead, "Sixth District Survey of Small Business Credit," Economic Review Federal Reserve Bank of Atlanta (April 1982), pp. 42-48.

Pam Frisbee contributed valuable research assistance in the preparation of this article. The author also wishes to thank the other District Federal Reserve Banks for their vital contributions. A longer, more detailed version of this study is available from the Information Center, Federal Reserve Bank of Atlanta.

1014000

Supreme Court of the United States

No. 84-1274

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, PETITIONER,

v.

DIMENSION FINANCIAL CORP., ET AL.

ORDER ALLOWING CERTIORARI. Filed *April 29, 1985*,

The petition herein for a writ of certiorari to the *United States Court of Appeals for the Tenth Circuit* is granted.

Justice White took no part in the consideration or decision of this petition.